

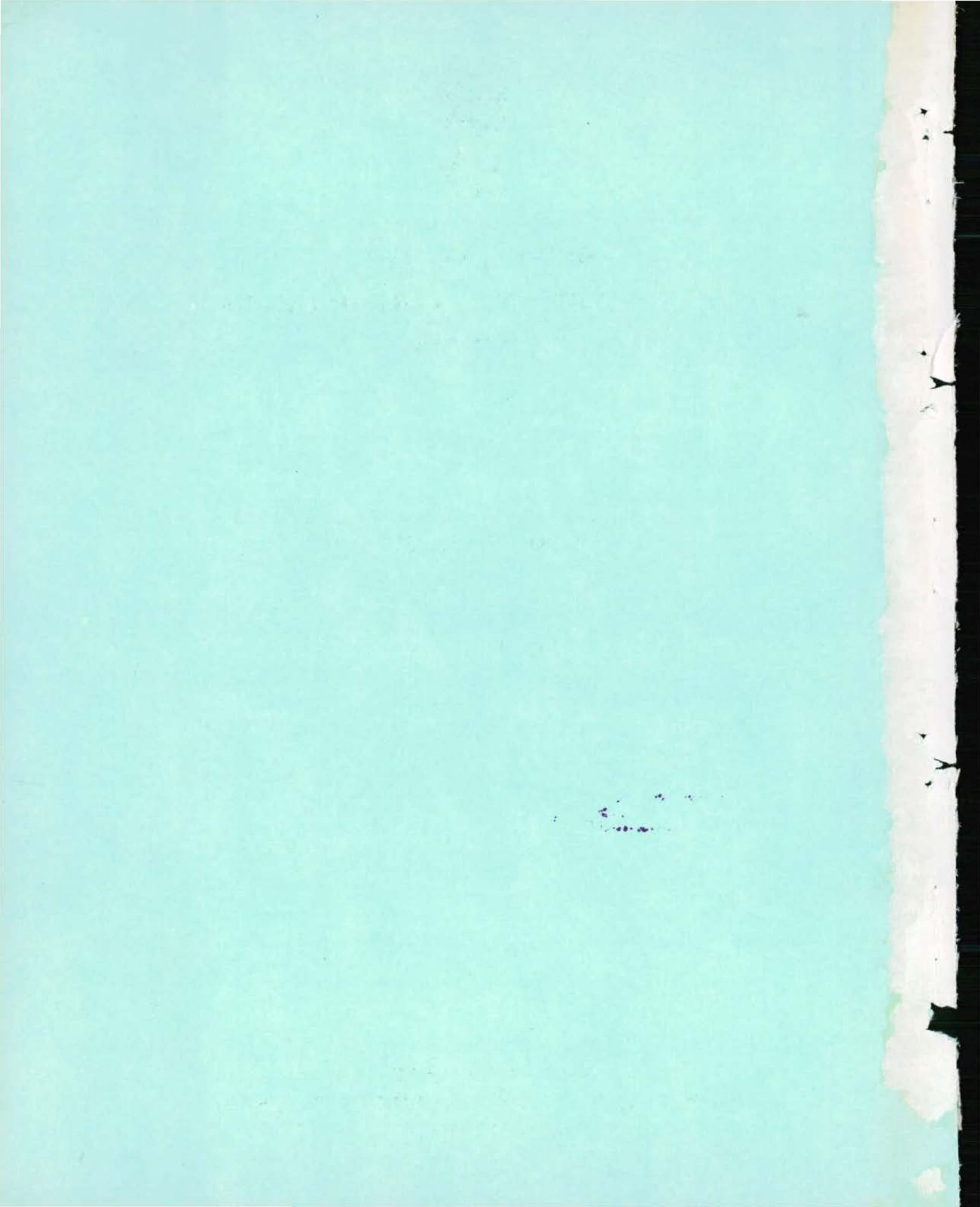


**REPORT OF THE  
COMPTROLLER AND AUDITOR GENERAL  
OF INDIA**

**FOR THE YEAR ENDED 31 MARCH 1996**

**NO.10 OF 1997**

**UNION GOVERNMENT  
REVENUE RECEIPTS - INDIRECT TAXES  
(CUSTOMS)**





सत्यमेव जयते

**REPORT OF THE  
COMPTROLLER AND AUDITOR GENERAL  
OF INDIA**

**FOR THE YEAR ENDED 31 MARCH 1996**

**NO.10 OF 1997**

लोक सभा/राज्य सभा  
के पटल पर.....  
को रखी गई।

114 मार्च 1997  
MAR

Rupees 100 (HINDI)  
US Dollar 5 Foreign

**UNION GOVERNMENT  
REVENUE RECEIPTS - INDIRECT TAXES  
(CUSTOMS)**

1901 - 11

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Dear Mother

Dear Mother

I received your letter of the 19th

and was glad to hear

from you and to hear that you were

well and that you were all

happy and contented

and that you were all

well and that you were all

well and that you were all

well and that you were all

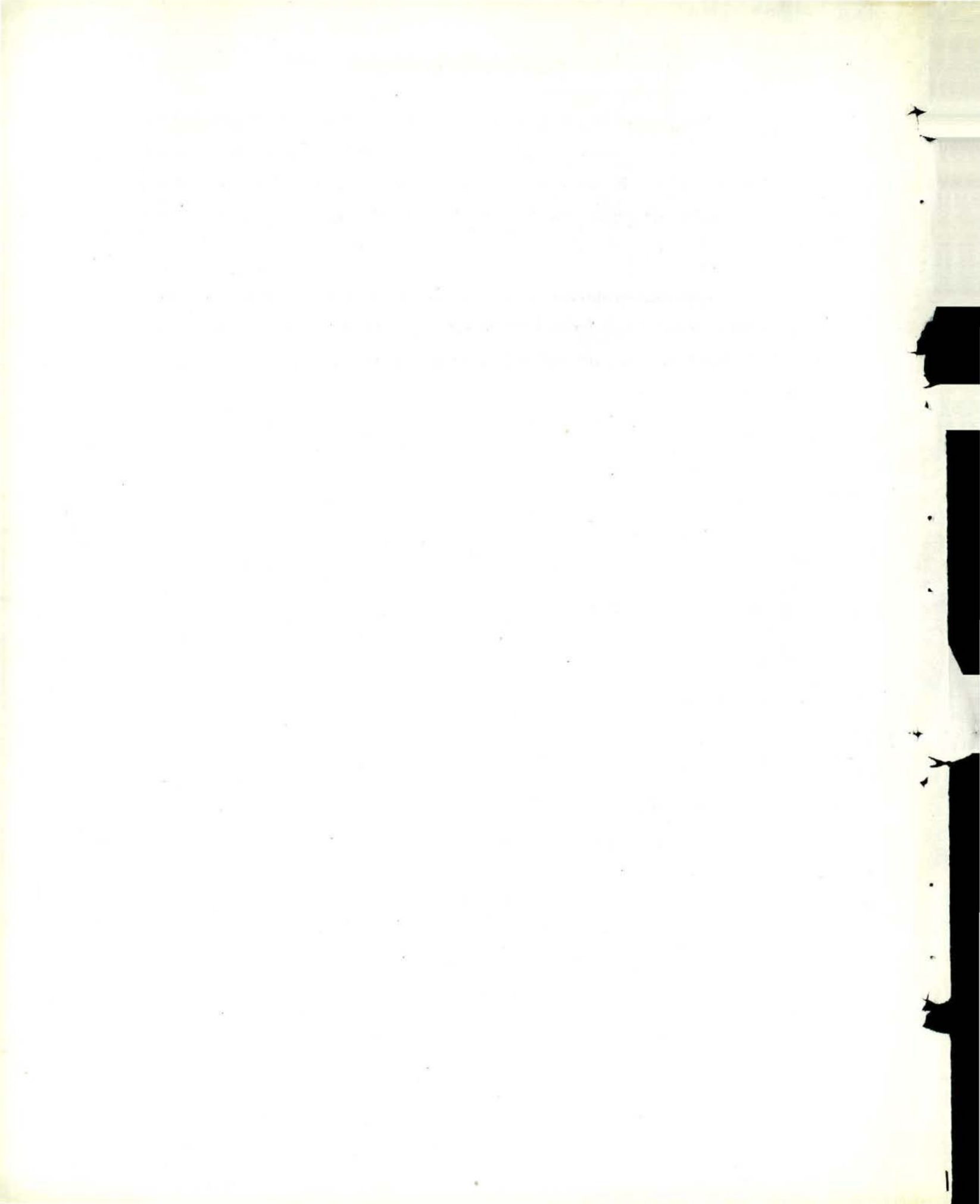
Yours affectionately

John W. [Name]

## **PREFATORY REMARKS**

This Report for the year ended 31 March 1996 has been prepared for submission to the President under Article 151 of the Constitution based on the audit of Customs 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.

The cases mentioned in the Report are among those which came to notice in the course of audit during 1995-96 and early part of 1996-97 as well as those which came to notice in earlier years but could not be reported earlier.





### Legends/Abbreviations used in the Report

Cash Compensatory Support	Referred as	CCS
Central Board of Excise and Customs	-do-	The Board
Commissionerate of Customs	-do-	Commissionerate
Cost, Insurance and Freight	-do-	cif
Custom House	-do-	The department
Customs duty	-do-	The duty
Customs Valuation (Determination of Price of Imported goods) Rules, 1988	-do-	Valuation Rules
Director General of Foreign Trade	-do-	DGFT
Director General of Health Services	-do-	DGHS
Domestic Tariff Area	-do-	DTA
Electronic Hardware Technological Parks	-do-	EHTP
Export Processing Zone	-do-	EPZ
Export Promotion Capital Goods	-do-	EPCG
Foreign Exchange Regulation Act, 1973	-do-	FERA
Foreign Trade (Development and Regulation) Act, 1992	-do-	FTDRA
Free on board	-do-	fob
Free Trade Zone	-do-	FTZ
Gem and Jewellery Units	-do-	GJUs
General Currency Area	-do-	GCA
Government of India	-do-	The Government
Harmonized Commodity Description & Coding Systems - Explanatory Notes	-do-	HSN
Hundred Percent Export Oriented Units	-do-	EOU
Importer Code Number	-do-	ICN
Legal Undertakings	-do-	LUT

Letter of Intent	Referred as	LOI
Letter of Permission	-do-	LOT
Madras Export Processing Zone	-do-	MEPZ
Mega Watt Hour	-do-	MWH
Metric Tonne	-do-	MT
Ministry of Finance	-do-	The Ministry
Modified Value Added Tax	-do-	Modvat
New Okhla Industrial Development Area	-do-	Noida
Noida Export Processing Zone	-do-	NEPZ
Public Accounts Committee	-do-	PAC
Public Sector Undertaking	-do-	PSU
Quantity Based Advance Licence	-do-	QBAL
Reserve Bank of India	-do-	RBI
Rupee Payment Area	-do-	RPA
Santa Cruz Export Processing Zone	-do-	SEEPZ
Secretariat of Industrial Approval, Ministry of Industries	-do-	SIA
Special Export Oriented Complex	-do-	SEOC
The Customs Act, 1962	-do-	The Act
The Customs Tariff Act, 1975	-do-	Tariff Act
Value Based Advance Licence	-do-	VABAL

## OVERVIEW

This report contains two reviews and 127 paragraphs involving non levy/short levy of customs duty of Rs.883.97 crores. Some of the important audit findings included in the Report are highlighted below:

### I GENERAL

The net receipts from customs duties during the year 1995-96 amounted to Rs.35,728 crores against the Revised Estimates of Rs.35,352 crores.

The average rate of customs duty came down from 46 per cent in 1991-92 to 31 per cent in 1993-94 and since then marginally declined to 29.37 per cent in 1995-96.

Customs duty of Rs.8,590 crores was forgone on imports made under 4 major export related schemes during 1995-96.

[Paragraph 1]

### II Review of 'Hundred per cent Export Oriented Units'

An appraisal of the Scheme of 'Hundred per cent Export Oriented Units' introduced by the Government in 1980 revealed.

— The customs duty recoverable from 48 units on account of shortfall in value addition worked out to Rs.215.94 crores.

[Paragraph 2.4]

— Non levy/short levy of customs and central excise duty on irregular DTA sales noticed in 36 units amounted to Rs.249.16 crores.

[Paragraph 2.5]

— Irregular exemption of customs duty on imports availed by 27 units worked out to Rs.12.62 crores.

[Paragraph 2.6]

— Customs duty forgone on inputs remaining unaccounted in 4 units amounted to Rs.15.10 crores.

[Paragraph 2.7.1]

— Irregular availment of Cash Compensatory Support, Drawback and reimbursement of Central Sales Tax by 14 units amounted to Rs.48.82 crores.

[Paragraph 2.7.3]

## OVERVIEW

### Gem and Jewellery Units

An appraisal of the 'Gem and Jewellery Units' setup in the Export Processing Zones at Santa Cruz, Noida, Madras and Cochin and the Special Export Oriented Complex at Jhandewallan, New Delhi revealed:

- Customs duty recoverable from 41 'Gem and Jewellery Units' on account of shortfall in value addition worked out to Rs.157.72 crores.

[Paragraph 3.4]

- 121 Kgs. of gold, valued at Rs.4.72 crores disbursed by MMTC to 11 units was not utilised for manufacture of jewellery for export, for which customs duty amounting to Rs.4.78 crores stood recoverable.

[Paragraph 3.5]

- System of divided and over-lapping responsibility of various authorities facilitated abuse of the scheme.

[Paragraph 3.6.5]

- For lack of co-ordination between the Development Commissioner, MMTC and Customs authorities the scheme is not being implemented satisfactorily.

[Paragraph 3.6.5]

- MMTC issued duty free gold to the units mostly on loan without any collateral security. Further, no verification to check utilisation of the gold already issued was being undertaken by MMTC before issue of further quantities.

[Paragraph 3.6.6]

- Contrary to Exim Policy, export obligation was treated as discharged on the basis of trading documents and not on the basis of foreign exchange realised. As per RBI records, foreign exchange amounting to Rs.57.65 crores remained unrealised for more than six months in respect of thirty units in SEEPZ and Noida.

[Paragraph 3.7]

### III IRREGULARITIES IN ASSESSMENTS

Short levy on account of undervaluation of assessable goods in 11 cases amounted to Rs.0.46 crore.

[Paragraph 4]

## OVERVIEW

In 25 cases, imported goods were incorrectly classified leading to short levy of Rs.1.09 crores.

**[Paragraph 5]**

Incorrect grant of exemption in 18 cases resulted in short levy of Rs.2.35 crores.

**[Paragraph 6]**

Non levy/short levy of additional duty in 45 cases, worked out to Rs.1.40 crores.

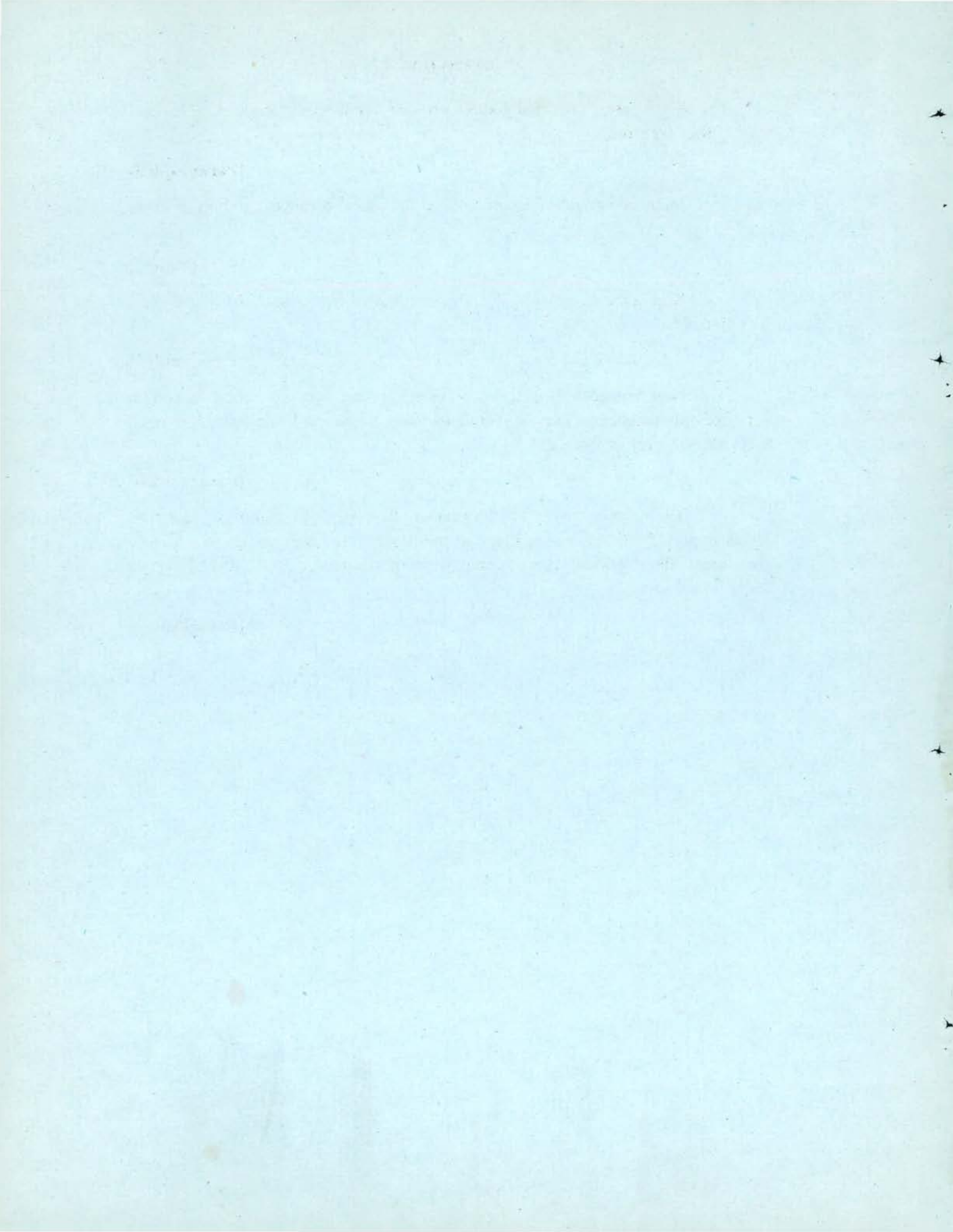
**[Paragraph 7]**

Non levy/loss of customs revenue, arising from operation of certain duty exemption schemes like Advance Licensing Schemes, EPCG etc., amounted to Rs.88.11 crores in 10 cases.

**[Paragraph 8]**

The revenue loss in 18 cases arising from cases like failure to re-export goods imported for exhibition, delay in remittance, re-warehousing, non levy of duty on pilfered goods, irregular payment of drawback etc., worked out to Rs.21.34 crores.

**[Paragraph 9]**



## 1. STATISTICAL INFORMATION

1.1 The customs revenues have witnessed a buoyancy in the recent past. This is attributable mainly to the rising trend in the imports following the liberalisation of the Indian economy. On the basis of the information furnished by Principal Chief Controller of Accounts, CBEC, the net receipts from customs duties during the year 1994-95 and 1995-96 (along with the budget estimates and the revised estimates for 1995-96) are shown in the table below.

Net Customs Receipts from	(Rupees in crores)			
	Actual Receipts 1994-95	Budget estimates 1995-96	Revised estimates 1995-96	Actual Receipts 1995-96
Imports	26003	29038	34702	34717
Exports	61	58	01	39
Cess on exports	80	96	105	116
Sale proceeds of confiscated goods	404	183	150	442
Other receipts	180	125	394	414
<b>Net receipts</b>	<b>26728</b>	<b>29500</b>	<b>35352</b>	<b>35728</b>

N.B. the figures shown have been arrived at after deducting refunds and drawback paid

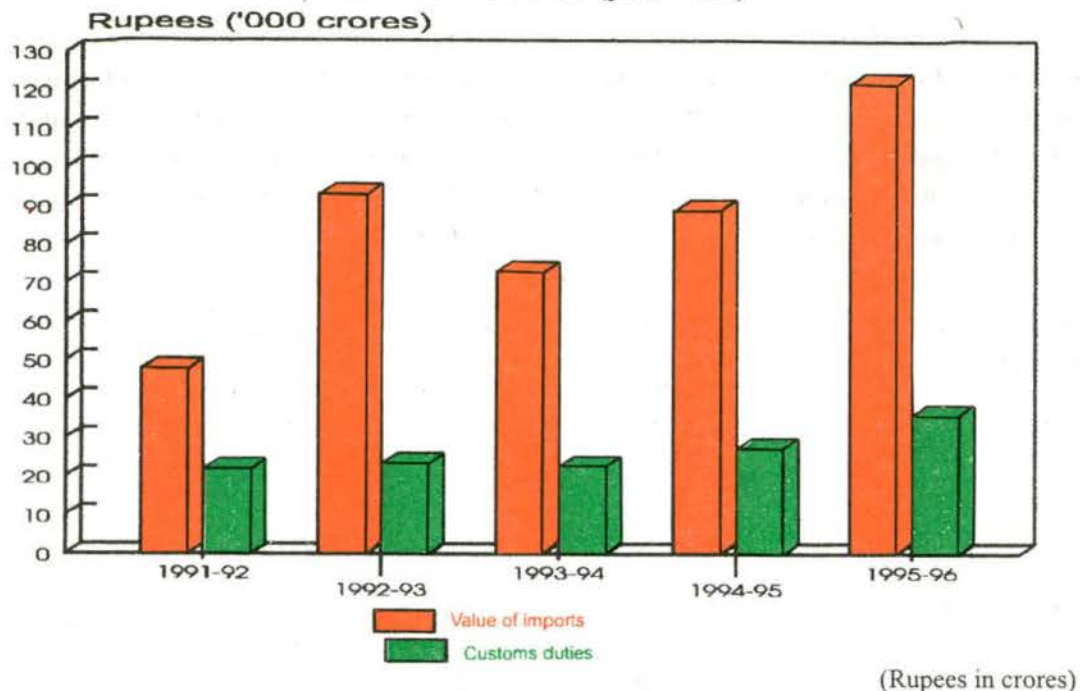
The increase in collection over estimates was mainly on account of higher revenue realisations from petroleum products, vegetable oils, machinery, iron and non alloy steel, copper, nickel, aluminium, zinc, inorganic chemicals, motor vehicles and parts, etc. The collection fell below estimates of duties from photographic and cinematographic goods, primary materials of iron and steel, lead, ball and roller bearings, project imports, etc.

The Ministry have confirmed the figures of net receipts.

### 1.2 Trend of receipts

A comparison of total year-wise imports with the corresponding customs duties collected during 1991-92 to 1995-96 has been shown in the bar chart and the table overleaf.

**Value of Imports and customs duty collected  
1991-92 - 1995-96 (year-wise)**



Year	Value of imports	Customs duties	Average rate of duty (Percentage)
1991-92	47851	21818	45.60
1992-93	62923	23323	37.07
1993-94	72806	22495	30.90
1994-95	88705	27148	30.60
1995-96	121647	35728	29.37

The rate of growth in the value of imports has been much higher than that of revenue between 1991-92 and 1995-96. The table above shows that the average rate of duty came down sharply from 46 per cent in 1991-92 to 31 per cent in 1993-94 and since then marginally declined to 29.37 per cent in 1995-96.

### 1.3 Commodity wise details of customs receipts

Major commodity wise value of imports and exports and the duty therefrom during the financial year 1995-96 and the previous year 1994-95 are given in the table over leaf:



**IMPORTS**

(Rupees in crores)

Sl. No.	Commodities	Value of imports		Import duties	
		1994-95	1995-96	1994-95	1995-96
1.	Petroleum (crude) & products	18629	25211	6209	8453
2.	Machinery (excluding machine tools) & their parts and accessories	8549	13242	2385	3475
3.	Electrical machinery	4206	7113	2116	2910
4.	Organic chemicals	4449	5747	2135	2514
5.	Project imports	5583	7528	1837	2028
6.	Motor Vehicles & parts thereof	3467	3619	697	1123
7.	Others	43822	59187	11769	15630
Total		88705	121647 @	27148	36133 (P)

(P) Provisional figures.

@ Subject to revision by the Ministry of Commerce.

**EXPORTS**

(Rupees in crores)

Sl. No.	Commodities	Value of exports		Export duty and cess	
		1994-95	1995-96	1994-95	1995-96
1.	Food items	11784	17969		6
2.	Beverages and Tobacco	255	366	10	8
3.	Crude materials inedible except fuels (including mica)	3974	5445	01	17
4.	Mineral, fuels, lubricant and related materials	1309	1518	—	—
5.	Chemicals and related products	10096	12621	—	—
6.	Manufactured goods classified according to materials except pearls, precious, semi precious stones and carpets, hand made leather and leather manufactures including readymade garments and clothing accessories	20922	25406	—	—
7.	Engineering goods	9480	12106	—	—
8.	Miscellaneous manufactured articles including handicrafts, gems and jewellery	21994	26494	—	—
9.	Others	2859	4540	127	81
Total of exports and re-exports		*82673	106465	138	112

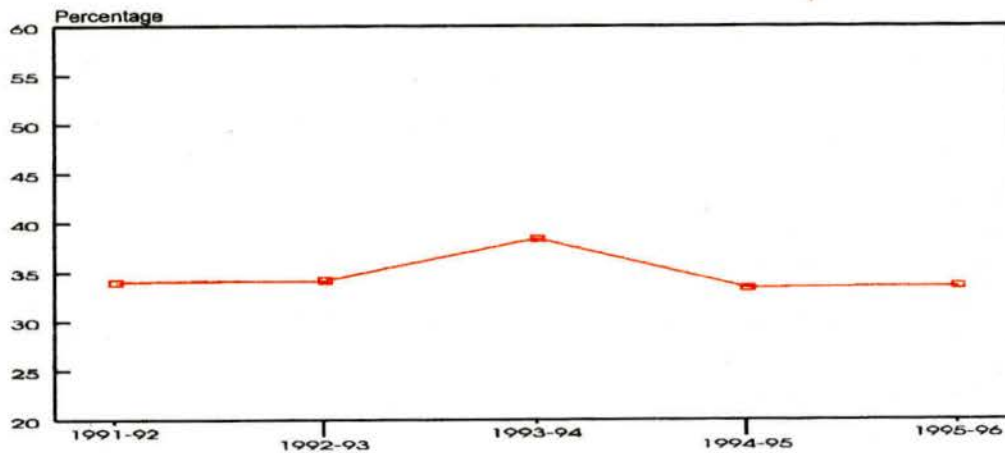
\*The figure of Rs.82338 crores indicated last year was updated by Ministry of Commerce.

It would be seen that the value of total imports had outstripped the value of total exports in both years. While the imports registered an increase of 37.14 per cent in 1995-96 over the previous year, the exports increased by 28.78 per cent in respect of the same period. This contributes to widening of the trade gap.

### 1.4 Commodity wise change in tariff levels

The following charts/tables show the changes in the average Tariff levels for the years 1991-92 to 1995-96 in respect of different product groups (arrived at by dividing the total import duty collected by the total CIF value of imports) in respect of six major commodities, viz. Petroleum (crude) and Petroleum Products, Machinery (excluding machine tools) and parts, Electrical Machinery, Organic Chemicals, Project Imports and Motor Vehicles and parts thereof. It may be mentioned that these commodities account for 56.74 per cent of the total customs revenue during 1995-96.

#### (a) Trend in average rate of duty for petroleum (crude) & products

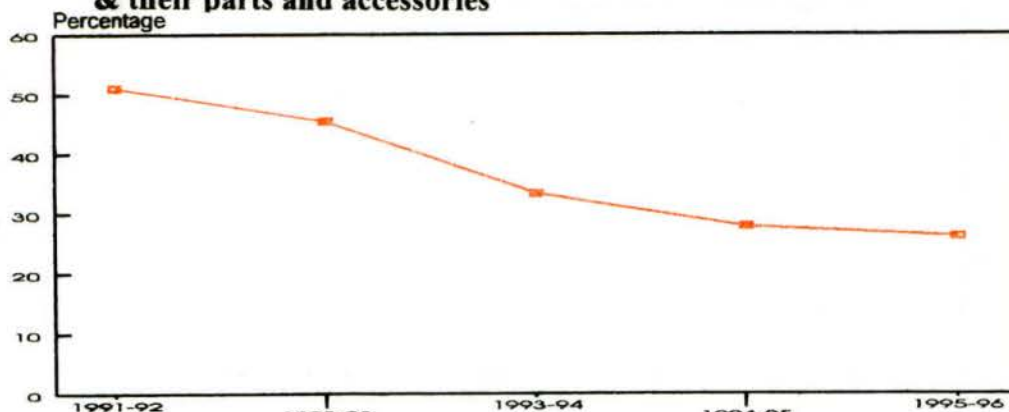


(Rupees in crores)

Year	Value of imports	Import duty	Average rate of duty (Percentage)
1991-92	13123	4441	33.84
1992-93	17153	5844	34.07
1993-94	18045	6914	38.32
1994-95	18629	6209	33.33
1995-96	25211	8453 (P)	33.53

(P) Provisional figures

**(b) Trend in average rate of duty for machinery (excluding machine tools) & their parts and accessories**

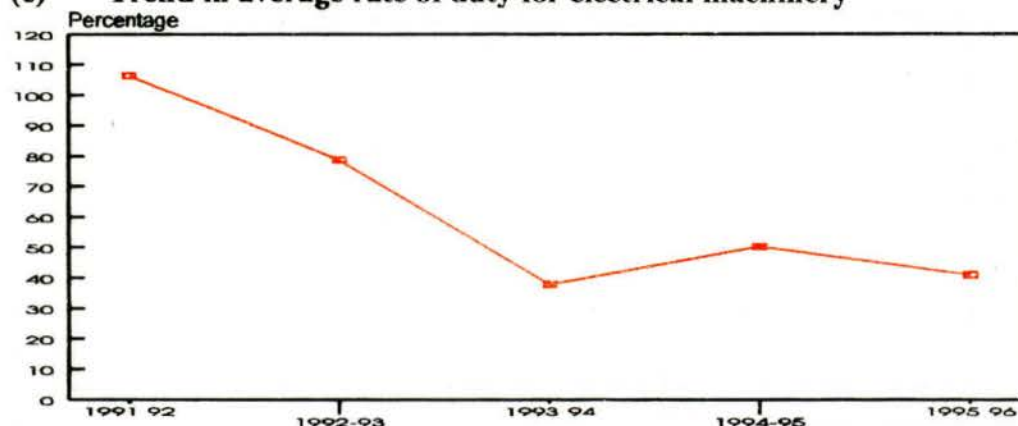


(Rupees in crores)

Year	Value of imports	Import duty	Average rate of duty (Percentage)
1991-92	3593	1835	51.07
1992-93	4865	2214	45.51
1993-94	5902	1971	33.40
1994-95	8549	2385	27.90
1995-96	13242	3475 (P)	26.24

(P) Provisional figures

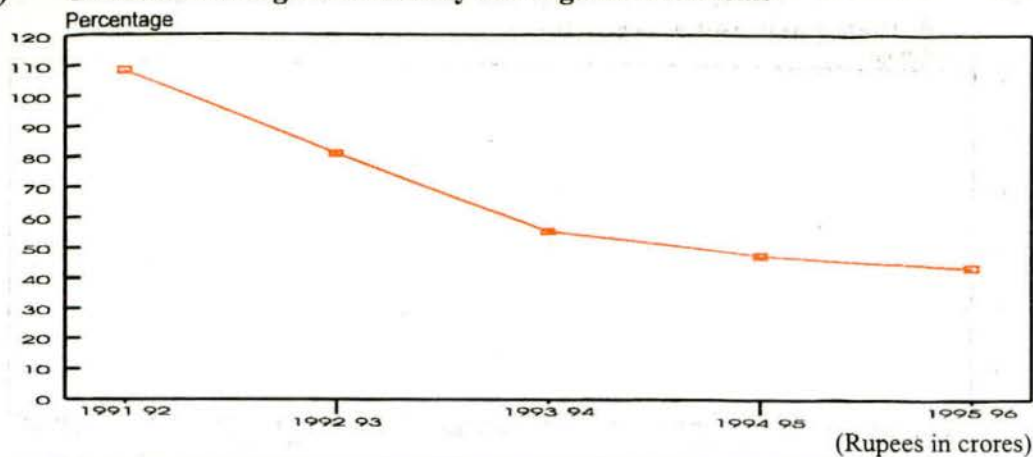
**(c) Trend in average rate of duty for electrical machinery**



(Rupees in crores)

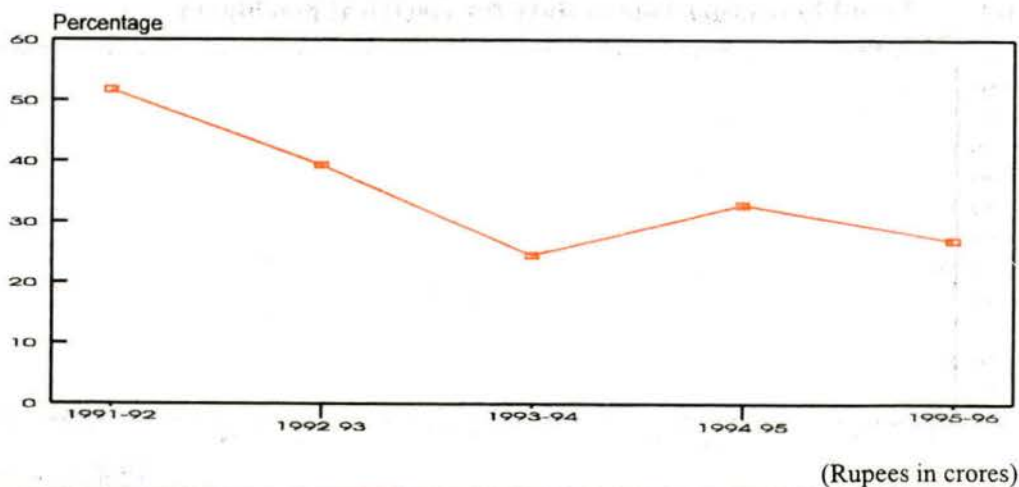
Year	Value of imports	Import duty	Average rate of duty (Percentage)
1991-92	1552	1654	106.57
1992-93	2358	1859	78.84
1993-94	3502	1328	37.92
1994-95	4206	2116	50.31
1995-96	7113	2910 (P)	40.91

(P) Provisional figures

**(d) Trend in average rate of duty for organic chemicals**

Year	Value of imports	Import duty	Average rate of duty (Percentage)
1991-92	1361	1479	108.68
1992-93	1977	1609	81.38
1993-94	2783	1553	55.80
1994-95	4449	2135	47.98
1995-96	5747	2514 (P)	43.74

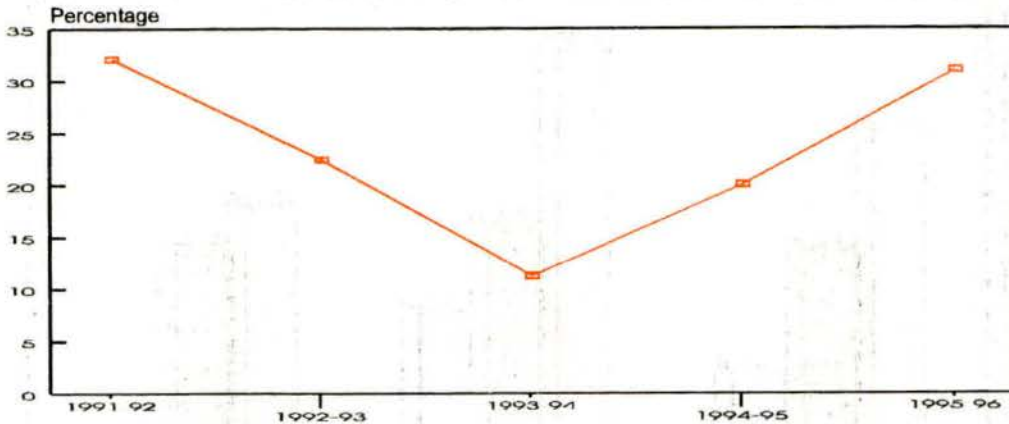
(P) Provisional figures

**(e) Trend in average rate of duty for project imports**

Year	Value of imports	Import duty	Average rate of duty (Percentage)
1991-92	3625	1874	51.70
1992-93	3460	1360	39.31
1993-94	5062	1242	24.54
1994-95	5583	1837	32.90
1995-96	7528	2028 (P)	26.93

(P) Provisional figures

## (f) Trend in average rate of duty for motor vehicles and parts thereof



(Rupees in crores)

Year	Value of imports	Import duty	Average rate of duty (Percentage)
1991-92	915	294	32.13
1992-93	1336	300	22.46
1993-94	3980	450	11.31
1994-95	3467	697	20.10
1995-96	3619	1123 (P)	31.03

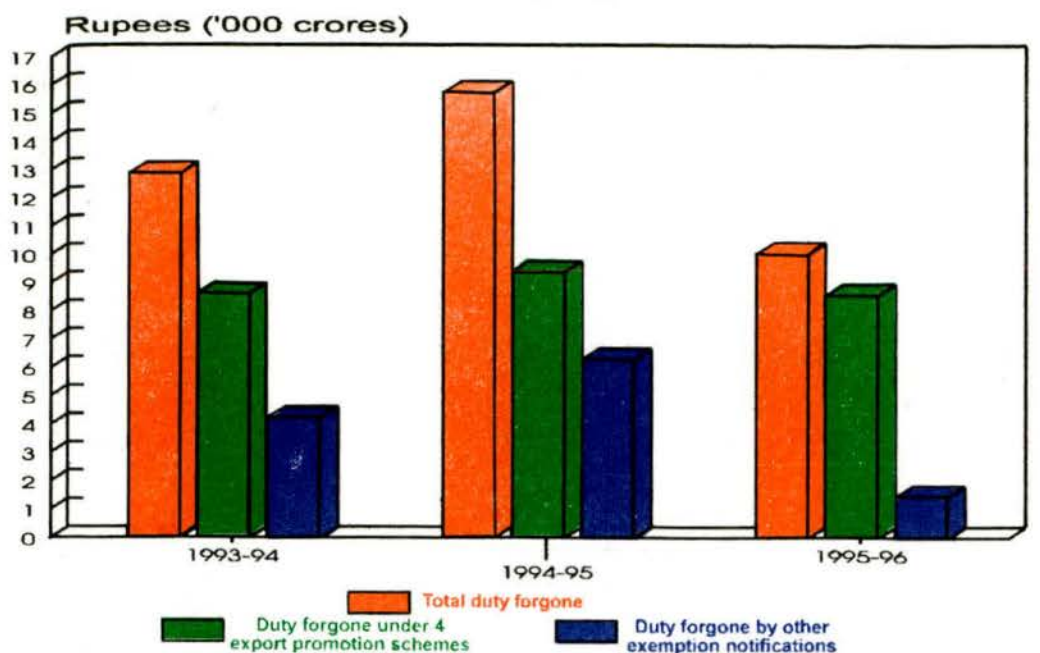
(P) Provisional figures

Notwithstanding the decline in rates of duty under these heads import duty collections have shown a rising trend for all these commodities due to a very sharp rise in the CIF value of imports especially in machinery, electrical machinery and project imports. Moreover, the policy of progressive reduction of customs duty was maintained upto 1993-94 after which there was an apparent shift in the policy. The rationale for such a change has not been made available to Audit.

## 1.5 Duty Forgone

1.5.1 Total duty forgone under various exemption notifications vis-a-vis the amount forgone in respect of four export promotion schemes viz., Advance Licence, EPCG, EPZ and EOU for the period 1993-94 to 1995-96 are shown in the bar chart and the table overleaf:

### Customs duty forgone



(Rupees in crores)

Year	Total duty forgone	Duty forgone under 4 export promotion schemes	Duty forgone by other exemption notifications
1993-94	12850	8605	4245
1994-95	15709	9390	6319
1995-96	10057	8590	*1467

\* Excludes duty forgone under Section 25(2)

It will be seen that during 1993-94 to 1995-96, the duty forgone under these four export related schemes was substantially higher than the total customs duty forgone under all other exemption notifications. However, the FOB value of exports relating to the 4 schemes which were introduced primarily for export promotion have shown satisfactory increase between 1993-94 to 1995-96 as would be evident from the table below:

### Fob Value of Exports under 4 Export Promotion Schemes

(Rupees in crores)

Year	Advance Licence	EPCG	EPZ	EOU	Total
1993-94	24812	2046	1960	3086	31904
1994-95	31241	4278	2653	4710	42882
1995-96	38423	16775	3236	6500 (E)	64934

(E) Estimated

1.5.2 The break-up of the duty forgone in respect of the four export promotion schemes viz., Advance Licence, EPCG, EPZ and EOUs for the period from 1993-94 to 1995-96 are shown in the table below:

**Customs duty forgone under 4 major export related schemes**

(Rupees in crores)					
Year	Advance Licence	EPCG	EPZ	EOU	Total
1993-94	4909	338 (appx)	1937	1421	8605
1994-95	5748	521 (appx)	1602	1519	9390
1995-96	4409	1023	1214	1944	8590

**1.5.3 Exemption notifications issued under Section 25 of the Act**

Duty forgone (other than in respect of four export promotion schemes vide para 1.5.2) during 1993-94 to 1995-96 are shown in the table below:

Year	No. of exemption notifications issued	Duty forgone (Rupees in crores)
1993-94	363	4245
1994-95	430	6319
1995-96	55	*1467

\* Excludes duty forgone under section 25(2)

**1.6 Cost of collection of customs receipts**

The expenditure incurred on collection of customs duty during the year 1995-96 alongwith the figures for the previous year are given below:

(Rupees in crores)			
Head of Accounts	Cost of collection	1994-95	1995-96
2037-101	Revenue cum import export and trade control functions	44.60	52.91
2037-102	Preventive and other functions	198.94	227.27
	<b>Total</b>	<b>243.54</b>	<b>280.18</b>
	Cost of collection as percentage of Customs receipts	0.88	0.76

The Ministry have confirmed the figures.

### 1.7 Searches, seizures and confiscations

The details of searches conducted and seizures effected by the Customs Officers as given by Ministry are indicated below:

#### (i) Searches and seizures

Sl.No.	Description	1994-95	1995-96
1.	Number of searches	*598	636
2.	Value of goods seized (Rs.in crores)	59	9
3.	Number of seizure cases adjudicated	380	1888

#### (ii) Confiscation

S.No.	Description	Number	Value (Rupees in lakhs)
1.	Motor Vehicles		
	(a) Confiscated during 1995-96	52	159.65
	(b) Pending disposal on 31 March 1995	1	1.64
	(c) Cleared during 1995-96	—	—
	(d) Balance on 31 March 1996	53	161.29
2.	Trade goods		
	(a) Confiscated during 1995-96	21	194.30
	(b) Pending disposal on 31 March, 1995	5	37.17
	(c) Cleared during 1995-96	20	43.07
	(d) Balance on 31 March, 1996	6	188.40

\*Note: The information in respect of Bombay, Kandla & Delhi Custom Houses has not been received.

### 1.8 Number of pending audit objections

The 4431 objections involving Rs.310.59 crores raised in audit upto 31 March 1996 were pending settlement as on 30 September 1996 in the various Custom Houses/Commissionerates.

### 1.9 Contents of the Report

This Report includes 127 paragraphs and two reviews on 'EOUs' and 'GJUs in the EPZs/SEOC', having a total revenue effect of Rs.883.97 crores. As of December 1996, the Ministry/Department have replied to 92 paras, accepting the audit observations involving Rs.5.85 crores.



## SYSTEMS APPRAISAL

### 2. Hundred per cent Export Oriented Units

#### 2.1 Introduction:

By a Ministry of Commerce resolution dated 31 December 1980, the EOU Scheme was introduced basically to boost exports, not merely by substitution but by creating additional production capacity. The scheme envisaged grant of duty free imports of capital goods and inputs on condition that hundred per cent output would be exported except for sale of specified allowable quantities in DTA. The scheme also envisaged specified percentage of value addition in fulfilling export obligations. The value addition is to be calculated according to the following formula given in para 119 of the Exim Policy 1992-97:

$$VA = \frac{A - B}{A} \times 100, \text{ where}$$

VA is value addition

A is the fob value of exports realised by the EOU unit

B is the sum total of the payments made in foreign exchange for goods and services.

Development Commissioners functioning under the Ministry of Commerce are responsible for monitoring the achievement of value addition and fulfilment of export obligations. Duty free imports of inputs are permissible in terms of notification No.13/81-Cus. under which the EOUs are required to execute a bond with the customs authorities to the effect that they would pay on demand an amount equal to the duty leviable on goods as were not proved to the satisfaction of the customs authorities to have been used in the manufacture of articles for export. In addition, exemption of Central Excise duty on indigenously procured capital goods and inputs and concessional duty on finished goods cleared in DTA were permitted by notification No.123/81-CE and No.169/90-CE as amended/superseded from time to time. Further, in terms of the Exim Policy, the units were obliged to submit an LUT to the concerned Development Commissioner. As per this undertaking, the units were liable to pay interest at the rate of 18 per cent (since revised to 24 per cent) on the duty found recoverable as well as liquidated damages equal to the value of the licence. No such interest could be charged by the Customs authorities in the absence of statutory provisions. In the case of EOUs covered in the test check, the interest liability could not be calculated/estimated in the most cases as complete information about dates of importation was not available.

Duality of control was thus introduced in the scheme. For a satisfactory implementation, well coordinated and concerted action by the Development

Commissioners and the Customs authorities were, therefore, necessary. The fulfilment of export obligation was being monitored by the Development Commissioner who had no authority to recover the duty. In case of any default, recovery action had to be initiated by the Customs authorities only.

To what extent, these concessions are instrumental in boosting exports will be available from the following data.

(Rupees in crores)

Year	cif value of imports	Customs duty forgone	CE duty forgone	fob value	fob value actually realised (US \$ in millions)
1991-92	392.69	—	*	1045.95	**
1992-93	923.09	1498.62	*	2170.13	**
1993-94	1076.36	1420.56	*	3086.05	**
1994-95	1214.63	1519.15	*	4709.59	**
1995-96	1350.00(E)	1943.59	*	6500.00(E)	**

\* The Ministry regretted their inability to furnish the figures as the data is not being maintained by them.

\*\* The Ministry of Commerce regretted their inability to furnish the figures as they are not monitoring the foreign exchange realisation.

(E) Estimated.

## 2.2 Scope of audit

An appraisal of the implementation of the EOU scheme was undertaken during October 1995 to July 1996. Records of seven Development Commissioners and those maintained by the concerned Commissionerates were test checked.

As per the information furnished by the Ministry of Commerce, 3369 EOUs were approved upto 31 March 1996, out of which 704 EOUs were functional. Of these, 381 EOUs were covered in test check.

## 2.3 Highlights

- i) **Customs duty exemption availed on import of capital goods and other materials corresponding to the short fall in value addition worked out to Rs.215.94 crores which was recoverable from 48 EOUs.**

[Para 2.4]

- ii) **Short levy/non levy of customs and central excise duties amounting to Rs.249.16 crores on irregular DTA sales was noticed in 35 EOUs.**

[Para 2.5]

iii) **Irregular exemption of customs duty amounting to Rs.12.62 crores was availed by 28 EOUs in respect of their imports in violation of the provisions of the Exim Policy and Customs notification.**

[Para 2.6]

iv) **Customs duty of Rs.15.10 crores was forgone on inputs remaining unaccounted in 4 EOUs.**

[Para 2.7.1]

v) **Irregular availment of Cash Compensatory Support and Drawback as well as reimbursement of Central Sales Tax amounting to Rs.48.82 crores was noticed in 14 EOUs**

[Para 2.7.3]

#### **2.4 Failure in achievement of value addition**

2.4.1 As the purpose of the scheme was basically to promote exports, paras 97 and 119 of the Exim policy 1992-97 prescribed certain percentages of value addition to the imported goods, while para 1(6) of the notification dated 9 February 1981 read with para 98 of the Exim Policy further prescribed recovery of the duty leviable on the imported goods as well as penalty in the event of failure of the units to achieve the stipulated value addition. Whereas monitoring achievement of the value additions and, in default, levy of penalty were within the jurisdiction of the Development Commissioners functioning under the Ministry of Commerce, the recovery of customs duty in case of shortfall in value addition was within the purview of the concerned Commissionerates.

2.4.2 Test check of records in 10 States under the jurisdiction of 5 Development Commissioners showed that 48 EOUs which had completed five years after the commencement of their commercial production had failed to achieve the required minimum value addition, resulting in shortfall to the extent of Rs.511.81 crores in value of exports. The duty forgone on the corresponding imports worked out to Rs.215.94 crores.

2.4.3 Out of the abovementioned 48 EOUs, shortfall in value addition worked out to Rs.258.45 crores in case of 7 EOUs which are briefly narrated below:-

(a) An EOU in Orissa manufacturing chrome using duty free imported chrome ore and coke achieved value addition of (-)14.40 percent over the specified period of 5 years as against 29 percent prescribed. This non achievement called for recovery of duty of Rs.62.06 crores and levy of penalty.

On the irregularity being pointed out (January 1992), the Development Commissioner stated (January 1996) that the case had been recommended for penal action to DGFT, New Delhi, whose decision is awaited. As regards recovery of duty, no information is available as to the action taken by the concerned Commissionerate as of December 1996.

(b) Another EOU in Orissa engaged in the manufacture of granite slabs and tiles, using duty free imported capital goods and raw-materials, failed to achieve the prescribed value addition for which recovery of duty of Rs.5.36 crores in addition to levy of penalty was called for. The Development Commissioner stated in January 1996 that the performance of the EOU was being watched. Recovery action by the concerned commissionerate was not known upto December 1996.

(c) An EOU operating under the Kanpur Commissionerate of Central Excise and producing cotton yarn could achieve a value addition of 14 per cent during 1990-91 to 1995-96 as against 31.24 per cent stipulated. This shortfall warranted recovery of duty of Rs.48.80 crores and levy of penalty. Reply of the Development Commissioner and the concerned Commissionerate are awaited as of December 1996.

(d) An EOU under the Meerut Commissionerate manufacturing Dot matrix printers, Floppy disk drive, etc. imported duty free capital goods, components, etc. but achieved value addition of 23.52 per cent between 1986-87 to 1991-92 as against 38 percent prescribed. The duty recoverable on account of this failure worked out to Rs.32.43 crores.

The Development Commissioner, Noida EPZ informed that a show cause notice had been issued in February 1996 and the matter reported to the DGFT in March 1996. Action taken for recovery of duty is still awaited as of December 1996.

(e) An EOU at Madras producing musical instruments achieved a value addition of 14 per cent against 43 per cent prescribed. This non-achievement called for recovery of duty of Rs.8 crores. Replies from the Development Commissioner and the concerned Commissionerate have not been received as of December 1996.

(f) An EOU under Indore Commissionerate approved for manufacture and export of leather products commenced production in April 1989 but closed down in December 1993 without fulfilling the prescribed value addition. The duty recoverable for this failure worked out to Rs.6.17 crores, in addition to penalty.

The DGFT, New Delhi stated (April 1996) that penalty of Rs.25 lakhs on the EOU and Rs.5 lakhs each on four partners had been imposed but the recovery particulars of custom duty are awaited as of December 1996.

(g) An EOU under Hyderabad Commissionerate engaged in the manufacture of special electrodes failed to achieve the prescribed value addition during 1991-92 to 1994-95. Customs duty of Rs.5.69 crores in addition to penalty was recoverable for the shortfall. The Development Commissioner issued an SCN to the EOU and referred the matter to the DGFT in June 1994 for further action. Further developments are awaited as of December 1996.

## **2.5 DTA sales**

In terms of para 102 of the Exim Policy 1992-97, EOUs are permitted, only after achieving the prescribed value addition, to sell in the DTA upto 25 per cent of their finished products, approved for manufacture and export with the exception of certain items like jewellery, diamonds, precious and semi-precious stones, silver, bullion, motor cars, etc.as are specified by DGFT. In addition, all EOUs are entitled to sell in the DTA, 5 per cent (or such percentage as may be fixed by the Board of Approvals) of the rejects and a specified percentage of the scrap/waste/ remnants arising from the manufacturing process.

Sale in DTA by EOUs is a post export entitlement to be availed within one year of its accrual which is, however, extendable. All DTA clearances are subject to payment of central excise duty at rates prescribed in terms of section 3 of Central Excise Act.

Test check of records revealed non-levy/short levy of central excise duty amounting to Rs.31.66 crores and customs duty amounting to Rs.217.50 crores in 35 units in 11 States as narrated below:-

### **2.5.1 Unauthorised DTA sales**

(a) An EOU in Orissa, manufacturing Charge Chrome, imported between February 1985 and May 1993 machinery and spares valued at Rs.145.12 crores for setting up a captive power plant. The duty exemption amounted to Rs.206.15 crores. The machinery was meant for generation of power required for manufacture of Charge chrome for export. Out of 29.32 lakh MWH of power generated by the captive plant during the period February 1989 to March 1995, only 6.57 lakh MWH was utilised by the EOU in manufacturing the goods for export, while the balance 22.75 lakh MWH (representing 77.60 per cent of the total generation) was sold by the EOU in the DTA for Rs.66.10 crores. Such sales were not reflected in the Annual Return of the EOU submitted to the Development Commissioner, Falta EPZ.

As 'Power' was not a product approved for manufacture and export by the EOU, such DTA sales were in violation of the scheme. The duty forgone on import of the machinery to set up the captive power plant was thus recoverable.

The matter was pointed out in audit in June 1992 following which the department issued, in February 1995, a demand cum show cause notice for Rs.214.43 crores. Recovery particulars are awaited as of December 1996.

The matter was referred to the Ministry in July 1995; their reply is awaited as of December 1996.

(b) An EOU under Ahmedabad Commissionerate sold its product valued at Rs.16.02 crores in DTA after availing a central excise duty exemption of Rs.4.64 crores during 1992-93 to 1994-95. As the EOU failed to achieve the prescribed minimum value addition during the said period, it was not entitled to any DTA sale. As a result, central excise duty of Rs.4.64 crores is recoverable. Action taken by the department is awaited as of December 1996.

(c) An EOU in Pune was granted LOI in September 1983 for manufacture of Sparkling Wine (Champagne) on condition that the finished product or the rejects would not be allowed to be sold in the DTA.

The EOU sold 54,973 bottles of liquor, valued at Rs.98.94 lakhs, in the DTA during 1992-93 to 1994-95 with the permission of the Development Commissioner, SEEPZ.

The Development Commissioner stated (March 1996) that the DTA sale permission was granted for the period 1990-91 to 1992-93 in accordance with the provisions of Para 102(b) of Exim Policy 1992-97 and the sale of alcoholic liquor in DTA is prohibited from 1 April 1993 only.

The reply is not relevant as the permission for such DTA sales was against the conditions of the LOI. As the conditions were violated the goods were liable to duty amounting to Rs.3.12 crores for recovery of which action should have been initiated.

(d) In terms of the provisions of the Exim Policy 1992-97, advance DTA sale could be permitted to an EOU only in case of trial productions subject to subsequent adjustment on accrual of DTA sale entitlement.

An EOU under Madras Commissionerate cleared tiles, availing central excise duty concession of Rs.1.21 crores as advance DTA sale during 1994-95 to January 1996 and was allowed to withdraw from the EOU scheme in December 1995 before fulfilling the export obligations. The issue of recovery of the duty exemption of Rs.1.21 crores from the unit has been referred to the concerned Development Commissioner and the Commissionerate; but no reply has been received as of December 1996.

(e) An EOU in Bangalore permitted to manufacture and export diesel generator sets, cleared diesel engines, valued at Rs.227.19 lakhs, in 1993-94 and 1994-95 in DTA at a concessional rate of duty. The unit has since been debonded and is working as a DTA unit from January 1995.

As the goods cleared in DTA were not the same permitted for manufacture for export, such clearance was irregular and a central excise duty of Rs.46.43 lakhs forgone on the aforesaid clearances was recoverable. This was pointed out in May 1996, reply is awaited as of December 1996.

(f) Six EOUs, two in Bombay, and one each in Guntur, Vadodara, Ahmedabad and Allahabad, failed to achieve the required minimum value addition but were allowed to make DTA sales of Rs.15.40 crores during 1991-92 to 1995-96 at concessional rates of central excise duty, resulting in unauthorised DTA sales and consequential short levy amounting to Rs.10.87 crores.

Action taken for the recovery of duty is awaited (December 1996).

(g) The Exim Policy 1992-97 prescribes that the DTA sale entitlement should be availed within one year of its accrual, which is extendable by another six months by the Development Commissioner of the concerned EPZ.

Five EOUs, three in Andhra Pradesh and one each in Gujarat and Madhya Pradesh cleared goods valued at Rs.168.04 lakhs in DTA during March 1992 to October 1995 either without permission or after expiry of the validity period of the permission, resulting in short levy of central excise duty amounting to Rs.35.03 lakhs.

In the case of the EOU in Madhya Pradesh, the Assistant Commissioner, Central Excise, Indore issued (November 1995) a show cause notice to the unit for recovery of Rs.13.65 lakhs. Further progress in this case and action taken in other cases are awaited as of December 1996.

### **2.5.2 Bunching of DTA sales**

In terms of Exim Policy 1992-97, any EOU manufacturing more than one product is permitted to sale its product in DTA subject to the condition that such sale in respect of any one product should not exceed either 25 per cent of total production of all items or 35 per cent of the production of the item being sold whichever is less.

(a) An EHTP unit under Meerut Commissionerate engaged in manufacture of different types of electronic goods, using materials imported duty free, exported only colour TVs and cleared the entire quantity of other manufactured goods worth Rs.5.58 crores in DTA at concessional rate of central excise duty. Since the

goods sold in the DTA were not identical to the goods exported and the individual items cleared in DTA exceeded the prescribed percentage, the concessional rate of duty was wrongly availed of. This resulted in a short levy of Rs.3.12 crores and was pointed out in January 1996. Action taken for the recovery is awaited (December 1996).

(b) Another EHTP unit under Meerut Commissionerate engaged in the manufacture and export of several electronic hardware products was permitted, with effect from 17 January 1995, to manufacture 'Pagers' which was not included as an item of manufacture for export in the bond executed by the unit.

Pagers valued at Rs.3.80 crores manufactured in 1994-95 were wrongly cleared in DTA at a concessional rate involving exemption of Rs.1.83 crores of central excise duty. The Director of Electronics stated in May 1996 that permission to sell Pagers was given under the provisions of bunching.

The reply does not address the two main issues viz., (i) the goods sold in DTA were not identical to the goods exported and (ii) that the total DTA sales exceeded the prescribed percentage.

No action to recover the duty has been initiated so far (December 1996).

(c) An EOU under Indore Commissionerate manufacturing different types of products cleared Synthetic yarn in DTA under the provisions of bunching in excess of the prescribed percentage during 1994-95. This resulted in irregular exemption of central excise duty of Rs.79.67 lakhs on the excess clearance. This was pointed out in October 1995. Action taken for the recovery of the duty is awaited (December 1996).

### **2.5.3 Excess DTA sales**

Five EOUs located under the jurisdiction of the Development Commissioners at Noida, Kandla, Madras and Vishakapatnam sold their products in DTA between 1991-92 to 1995-96 in excess of the prescribed percentage of production while availing concessional central excise duty. Although the total value of such excess DTA sales was Rs.5.38 crores, the duty recoverable on excess DTA sales worked out to Rs.2.31 crores in respect of four EOUs. The duty recoverable in remaining in one EOU could not be worked out. One of these EOUs located in Madras was wholly engaged in DTA sales, without any export. Action taken for recovery is awaited (December 1996).

### **2.5.4 Irregular duty concession on DTA sales**

In terms of notification No.13/81-Cus., where non excisable articles produced by an EOU are allowed to be sold in India, duty at appropriate rate shall be levied on inputs imported duty free and used for manufacture of such articles.



(a) An EOU in Tarapur (Maharashtra) sold 1,17,000 cubic meter of Helium in DTA during 27 September 1991 to 1 June 1995. No excise duty was levied as the goods were non-excisable. But the duty leviable on inputs as per abovementioned provision worked out to Rs.2.70 crores and was recoverable. This was pointed out in April 1996. Action taken for the recovery is awaited (December 1996).

(b) An EOU in Kerala manufactured mineral water using PET bottles imported duty free and cleared the product in DTA during August 1993 to March 1995 on payment of concessional rate of central excise duty on PET bottles. Since mineral water was non-excisable upto 16 March 1995, customs duty of Rs.37.25 lakhs leviable on the imported PET bottles was recoverable. This was pointed out in February 1996. Action taken for the recovery is awaited (December 1996).

### 2.5.5 Rejects

In terms of para 102(a) of the Exim Policy 1992-97, rejects upto 5 per cent of production or such other percentage as may be fixed by the Board of Approvals can be cleared for DTA sales on payment of concessional duties.

(a) An EOU under Madras Commissionerate manufacturing acid resistant tiles, cleared rejects on payment of concessional rate of central excise duty in excess of the permissible limit of 5 per cent of their production on the basis of permission granted by the Ministry of Industry. Duty leviable on the excess quantity cleared amounted to Rs.1.01 crores. This was pointed out in April 1996 but the reasons for granting such a benefit had neither been explained nor the recovery particulars been made available (December 1996).

(b) An EOU under Guntur Commissionerate engaged in the manufacture of polished granite slabs, cleared sawn granite slabs, valued at Rs.82.69 lakhs as waste and remnants during 1991-92 to 1994-95 without paying Rs.85.14 lakhs of central excise duty leviable.

On this being pointed out, the department contended that the goods cleared in DTA were remnants/rejects of raw materials and were non-excisable. The department's reply is not tenable as the goods cleared were excisable as per clarification issued under the Central Excise Collectorate Bombay-I Trade Notice No.7/87. Action taken for the recovery of the duty is awaited (December 1996).

(c) Another EOU under Hyderabad Commissionerate engaged in the manufacture of polished granite slabs, cleared rejects in excess of 5 per cent at concessional rate of excise duty during 1993-94 to 1995-96 without any permission from the Board of Approvals. The clearance of excess quantity valued at Rs.10.79 lakhs resulted in short levy of central excise duty of Rs.3.98 lakhs.

On this being pointed out in August 1995, the department stated that the assessee was earlier getting permission from the Development Commissioner for the clearance of rejects in excess of 5 per cent and that the concessional rate of duty would also be applicable to the clearances in excess of the aforesaid ceiling. The reply is not tenable as the Development Commissioner is not competent to fix percentage of rejects in excess of 5 per cent for clearance in DTA.

(d) An EOU in West Bengal sold in the DTA 2059.5 lts. of paints, 336 lts. of thinner and 143 sets of plywood imported duty free, without any further processing, during 1992-93 to 1994-95. Duty amounting to Rs.0.19 crores which was forgone on the said materials was thus recoverable. Action taken by the department has not been reported as of December 1996.

### **2.5.6 Other irregularities**

(a) In terms of the relevant notifications, concessional rate of excise duty is leviable on all DTA clearances made in accordance with the conditions of the Exim Policy. Such concessional rate of duty is however not applicable to the goods falling under the Negative List of Imports in the Policy. An EOU in Gujarat was allowed DTA sales of "Unbleached plain, woven fabrics", valued at Rs.23.05 lakhs, during April-June 1995, on payment of concessional duty. Another EOU in Haryana sold 84 CTV sets in DTA for Rs.4.41 lakhs during April-May 1995 also on payment of concessional duty. As the aforementioned goods, falling under the Negative List of Imports in the Exim Policy, were not eligible for the concessional rate of duty, a short levy of Rs.7.41 lakhs resulted. Action taken for the recovery of the duty is awaited (December 1996).

(b) Four units, one each in Coimbatore, Ludhiana, Indore and Calcutta, cleared waste valued at Rs.6.11 crores during 1993-94 to August 1995 without payment of the concessional duty leviable. The non levy worked out to Rs.78.72 lakhs in these cases. Action taken for the recovery of the duty is awaited (December 1996).

### **2.6 Irregular imports - non levy of duty**

Duty free imports of capital goods and other materials by an EOU is allowed subject to certain conditions, some of which are:

- i) that the items imported are specifically covered under customs notification No.13/81 at the time of import,
- ii) that the importer has been granted necessary licence;
- iii) that the imported goods are utilised for manufacture/packaging of finished goods or development of software in bonded premises;
- iv) that the importer executes a bond as already discussed in para 2.1 (supra).

A test check of records revealed that 28 EOUs were allowed duty free imports in violation of one or more of the aforementioned conditions prevailing on the date of importation. This resulted in irregular exemption of duty amounting to Rs.12.62 crores. Details of such cases are given in the succeeding paras 2.6.1 to 2.6.3.

### **2.6.1 Capital goods not covered by exemption**

(a) 'Diesel generating sets' were not eligible for duty free import under the relevant notification till 12 June 1990.

12 EOUs, five of Madras, three of Calcutta and one each of Kandla, Vadodara, Ahmedabad and Kanpur, were allowed duty free imports of the aforesaid item through 6 Commissionerates before 12 June 1990. This resulted in non levy of duty of Rs.2.52 crores.

The reply of the department is awaited (December 1996).

(b) Material handling equipments namely Fork Lift and Over-head Cranes had been allowed duty free import with effect from 19 March 1984 and spares of capital goods and material handling equipments also came under the purview of exemption from 1988-89.

3 EOUs were allowed duty free imports of material handling equipments and spares through a major Custom House before these were eligible for duty free importation resulting in non levy of duty of Rs.0.44 crore.

Action taken for recovery of the duty is awaited (December 1996).

### **2.6.2 Import of goods in excess of permissible limits**

Value of imports to be allowed duty free are indicated in the LOI granted by the Board of Approval. It was noticed that 5 EOUs under four Commissionerates, viz., Meerut, Goa, Bombay and Surat were allowed import of goods valued at Rs.4.46 crores in excess of the permitted limit. This resulted in non levy of duty of Rs.3.38 crores on excess imports.

The reply of the department is awaited (December 1996).

### **2.6.3 Other irregularities**

(a) In December 1994, an EHTP unit under Meerut Commissionerate, was allowed duty free import of components of Diagnostic ultra sound scanners - Module sonoace 1500, Main body with a built-in monitor 3.5 MHZ Convex probe standard accessories for export after calibration and testing. As calibration and testing did not amount to manufacture, the duty free import allowed to the unit was irregular. The duty not levied on the abvoementioned goods amounted to Rs.2.48 crores. Action taken to recover the duty is awaited (December 1996).

(b) Under the Exim Policy 1985-88 read with the relevant notification, duty free import of more than 7 year old machinery was not permissible.

Out of 124 knitting machines imported duty free by an EOU in Punjab through a major Custom House, 19 machines were more than 7 years old as per certificate issued by the Chartered Engineer. Thus, in terms of the aforesaid provisions, such import was irregular and duty amounting to Rs.0.11 crore should have been levied. Action for recovery has not been reported as of December 1996.

(c) The Exim Policy further stipulates that with effect from 1 July 1982 imports by an EOU will not be cleared in the absence of a valid ICN.

An EOU in Punjab imported capital goods valued at Rs.121.00 lakhs without payment of duty during August 1987 to June 1988, prior to the allotment of ICN. This resulted in irregular availment of exemption of duty of Rs.1.71 crores. This was pointed out in February 1996 but recovery particulars are awaited as of December 1996.

(d) Two EOUs of Gujarat were granted irregular exemption of Rs.1.41 crores on imports of spares and raw materials in excess of the amounts covered in the legal undertakings executed by the units and on import of "cotton", a restricted item, without a valid import licence. The irregularity was pointed out in February and April 1996 respectively but recovery particulars are awaited (December 1996).

(e) An EOU, engaged in software development in Karnataka, imported (August 1993) goods valued at Rs.16.46 lakhs availing duty exemption of Rs.21.86 lakhs. But as per entries made in the Bond Register, the above mentioned goods were not actually received in the bonded area, indicating diversion of the goods. Although such violation called for recovery of duty in addition to levy of penalty, no action has been initiated as of December 1996.

(f) In terms of the relevant notification, a valid licence is a pre-requisite for duty free import of goods by an EOU.

An EOU in Tamil Nadu imported 'Prisms' and 'Lenses' between December 1993 and June 1994 without payment of duty although such items were not included in its licence. The duty free import was therefore, irregular and duty of Rs.0.16 crore stood recoverable from the EOU. This was pointed out to the department in April 1996; their reply is awaited (December 1996).

(g) An EOU under the Meerut Commissionerate manufacturing readymade garments, was granted LOP for 10 years from April 1983. Subsequently, on 29 October 1984, the name of the EOU was changed on condition that the validity of the LOP would not be extended beyond March 1993.

It was found that the EOU imported capital goods worth Rs.8.30 lakhs and raw materials worth Rs.16.04 lakhs without payment of duty during September 1993 to February 1995. The incidence of customs duty on these imports worked out to Rs.0.19 crore, the recovery of which has not been initiated (December 1996).

## **2.7 Other topics**

Certain issues like shortages of stock, incorrect computation of export achievements, non realisation of foreign exchange and grant of inadmissible benefits have been discussed in the succeeding paras 2.7.1 to 2.7.4. Irregularities that came to notice as a result of test audit shows that duty of Rs.71.35 crores is recoverable in 20 cases under 6 Development Commissioners.

### **2.7.1 Shortages of stock**

(a) An EOU in Orissa which was taken over by the State Government and subsequently sold to a Company 'A' on 27 September 1991, had (as of 26 September 1991) a closing stock of 8756 tonnes of duty free imported coke. Company 'A', after physical verification, took over only 7107 M.T. of coke, indicating a shortage of 1649 M.T. on which Rs.39 lakhs of duty was forgone. As the abovementioned amount of 1649 M.T. of coke was evidently not utilised for manufacture of goods for export, Rs.39 lakhs of duty forgone on its importation is recoverable. But as the ownership of the EOU changed twice before detection of the shortage, it is incumbent upon the department first to determine as to who is liable to pay the duty and then initiate recovery proceedings. Although this was pointed out to the department in February 1996, action to initiate recovery proceedings have not been reported till December 1996.

(b) An EOU in Tamil Nadu which produced 780794 sq.ft of polished granite slabs between 1987-88 and December 1995, exported 608370 sq.ft of the product. As no other clearances were made during the aforesaid period, the closing stock as on 31 December 1995 should have been 172,424 sq. ft, against only 9911 sq.ft. shown by the unit in their return to their Bankers. 162513 sq.ft. granite slabs thus remained unaccounted, for which duty of Rs.13.39 crores stands recoverable. The matter was brought to the notice of the department in March 1996; their reply is still awaited (December 1996).

(c) In two other cases, one each in Tamil Nadu and Orissa, there was a shortage of stock on which duty amounting to Rs.1.32 crores was recoverable.

Actions taken for recoveries of duty are awaited (December 1996).

**2.7.2 Incorrect counting of export achievements**

With effect from 13 August 1993, consultancy fees received in convertible foreign currencies for consultancy services rendered abroad by EOUs engaged in the development of software, are to be counted towards fulfilment of export obligation.

An EOU in Madras, engaged in the development of software and claiming an export performance of Rs.6.27 crores for consultancy services rendered abroad, actually realised Rs.1.61 crores in foreign currencies. As such, its export performance was overstated by Rs.4.66 crores, resulting in a value addition of (-) 54.8 per cent as against 60 per cent prescribed. The duty amounting to Rs.2.49 crores which was forgone on the imported capital goods and consumables was, therefore, recoverable. The reply of the department is awaited (December 1996).

**2.7.3 Irregular grant of other export benefits**

In terms of Resolutions of 31 December 1980 and 21 November 1983 of the Ministry of Commerce, benefits such as CCS, Replenishment Licences, etc. were not admissible for exports made by the EOUs. In addition, no drawback was payable to the EOUs in terms of General Note 2(e) of the Public Notice under which the All Industry Rates of Drawback are notified annually by the Ministry. The following illustrative cases noticed during test audit would reveal violation of the abovementioned circulars:

- (a) Three EOUs in Gujarat were paid Rs.2.06 crores as CCS for exports made during 1985-86 to 1992-93.
- (b) One EOU under Kanpur Commissionerate was paid Rs.51.30 lakhs as CCS and Rs.4.95 crores as reimbursement of Central Sales Tax during 1991-92 and 1992-93.
- (c) Seven EOUs under the jurisdiction of the Development Commissioner, SEEPZ had been paid CCS of Rs.40.40 crores during 1988-89 to 1994-95.
- (d) Three other EOUs under the jurisdiction of the Development Commissioner, SEEPZ had been paid drawback of Rs.0.90 crore on their exports made during 1989-90 to 1994-95.

Action taken for the recovery of the amount of such irregular disbursements is awaited (December 1996).

**2.7.4 Other irregularities**

In terms of para 3 of notification No.13/81-Cus., an EOU engaged in the development of computer software was entitled to the benefit of the EOU scheme.

The Ministry of Industry granted approval in June 1994 for setting up an EOU for data management and information processing. This unit was found to be a centre for processing raw data received from business offices of the company outside India and exporting the aforesaid processed data. Although such processing amounted neither to manufacture or packaging of goods for export nor to development of software, the EOU was allowed to import capital goods valued at Rs.6.67 crores, availing duty exemption of Rs.4.94 crores upto December 1995. Since the EOU was not eligible for such exemption, duty forgone on the importation of the above mentioned capital goods stands recoverable.

2.8 The basic objective of the scheme as stated earlier was to boost exports and thereby augment the foreign exchange resources. However, no mechanism was evolved by Ministry of Commerce to monitor the realisation of export sale proceeds by the EOUs in order to assess the actual generation of additional foreign exchange. As per the formula of value addition, the fob value of export **realised** should be taken into account. However, it was noticed that the Development Commissioners were relying on the trading records (i.e. the value declared on the shipping bills) instead of the payment records (i.e. records relating to actual remittances) for determining the discharge of export obligation. It has been admitted by the Ministry of Commerce that they are not monitoring the realisation of foreign exchange under the scheme. This is an important area which needs to be addressed for achieving the basic objective of the scheme.

2.9 The irregularities contained in this Review (para 2.1 to 2.7) were brought to the notice of Ministry of Commerce and Ministry of Finance in October 1996; their replies are awaited (December 1996).

## GEM AND JEWELLERY UNITS IN E.P. ZONES

### 3.1.1 Introduction

In order to boost exports and improve the foreign exchange earning, a Scheme to set up Free Trade Zones (later named as EPZs) was envisaged by the Government in 1965. The basic feature of the Scheme was to grant duty free imports by approved units located in specified zones on condition that the entire production of the units would be exported. Another feature of the scheme was that the units were to attain specified value additions on fulfilment of their export obligations. The EPZs are demarcated customs bonded areas with restrictions, on movement of goods to and from the DTA. In the year 1987-88, the Scheme of EPZs was extended to the 'Gem and Jewellery' sector. Initially, 105 GJUs were allowed to be set up in the EPZs at Santa Cruz, Noida, Madras and Cochin. Besides these units, an SEOC for manufacture of jewellery was set up at the

Jhandewalan Complex, New Delhi in 1988. Under this extended scheme, the GJUs were permitted to import gold, precious metals and stones, capital goods, tools, office equipments, packaging materials, etc., free of duty. The units were required to execute a bond with the Customs authorities agreeing to comply with conditions governing the scheme or, for default, to pay the duty exemption availed. Further, in terms of the Exim Policy, the units were obliged to submit a legal undertaking to the concerned Development Commissioner. As per this undertaking, the units were also liable to pay interest at the rate of 18 per cent (since revised to 24 per cent) on the duty found recoverable as well as liquidated damages equal to the value of the licence. No such interest can be charged by the Customs authorities in the absence of statutory provisions. In case of GJUs test checked, the interest liability could not be calculated/estimated in most cases as complete information about the dates of importation etc., were not available.

3.1.2 While the terms and conditions for imports by the GJUs are prescribed in the relevant Customs notifications issued from time to time, the Exim Policy lays down the conditions under which the EPZ/SEOC units are to function. Some of the important conditions of the Exim Policy are as under:

- i) As per para 97 read with 119 of the Policy, the units are required to achieve specified value additions and discharge their export obligations.
- ii) In terms of para 102 of the said policy and relevant customs notifications, the GJUs are neither permitted to remove the imported gold out of the EPZ nor sell the jewellery manufactured by them (including the waste, refuse and rejects) in the DTA.
- iii) In the event of any GJU ceasing its operation, the closing stock of gold, other precious metals, alloys, gems and other materials are to be handed over to an agency nominated by the Ministry of Commerce for the purpose.
- iv) The GJUs are required to maintain proper accounts of import, consumption and utilisation of the imported material and of exports. Such accounts are also required to be submitted to the Assistant Commissioner of Customs.

Development Commissioners, functioning under the administrative control of the Ministry of Commerce, are responsible for monitoring the fulfilment of export obligation of the GJUs. They are also empowered to initiate penal action for any default of the GJUs under the provisions of Foreign Trade (Development and Regulations) Act, 1992 and the rules and orders made thereunder. The Customs department, on the other hand, is responsible for monitoring proper utilisation of the imported gold, removal of the finished jewellery from the EPZ and recovery of duty from the importers in case of any violation.



3.1.3 In June 1988, the Ministry of Commerce formulated a scheme for supply of gold and gold ingredients by MMTC to the GJUs either on loan or on outright sale basis on condition that the finished jewellery should be exported to achieve the minimum prescribed value addition within a period of 90 days (reduced to 60 days with effect from February 1996). The conditions governing this scheme are laid down in the Customs notifications No.3/88 and 177/94 and Ministry of Commerce REP Circular No.22/88. The Customs notifications permit MMTC to import gold free of duty as an agent for the GJUs, who are required to furnish a bond agreeing to comply with the conditions and stipulations of the EPZ Scheme. However, according to the REP Circular No.22/88 of the Ministry of Commerce, MMTC was the primary importer having title to the gold, which was either sold or given on loan to the GJUs. The difficulties arising in implementation of the scheme from the contradictions between the Customs notifications and the REP Circular have been highlighted in para 3.6 (infra).

3.1.4 A total quantity of 23382 Kgs. of imported gold was issued by MMTC either on loan or on outright sale during the years 1988-89 to 1995-96 in the four Export Processing Zones (Santa Cruz, Noida, Madras and Cochin) and at Jhandewalan (New Delhi), the details of which are given below:

#### GOLD ISSUED BY MMTC

(In Kilogrammes)

Year	SEEPZ		NEPZ		MEPZ		Cochin		JHA		Total	
	Loan	Out-right Sale	Loan	Out-right Sale	Loan	Out-right Sale	Loan	Out-right Sale	Loan	Out-right Sale	Loan	Out-right Sale
1988-89	0	0	0	0	60	6	0	0	154	0	214	6
1989-90	108	14	0	0	5	5	0	0	527	24	640	43
1990-91	317	61	0	0	20	0	0	5	684	0	1021	66
1991-92	968	147	243	0	15	0	15	15	829	44	2070	206
1992-93	1669	174	1364	0	26	0	10	10	1006	0	4075	184
1993-94	2233	57	1318	0	10	0	35	0	682	0	4278	57
1994-95	2594	399	2218	0	18	0	10	0	333	0	5173	399
1995-96	1943	1138	1423	6	27	0	0	0	408	5	3801	1149
Total	9832	1990	6566	6	181	11	70	30	4623	73	21272	2110

**Grand total = 23382 Kgs.**

Details of the export of gold jewellery, manufactured out of the abovementioned 23382 Kgs. of gold was not made available to audit, although MMTC was required to obtain such data from the GJUs. MMTC has also not furnished the figures relating to the total customs duty forgone on the 23382 Kgs. of imported gold. On the basis of the quantity of gold imported each year and the rate of duty prevailing during that year, the total duty forgone has been estimated to be Rs.850 crores approximately.

### 3.2 Scope of audit

In order to assess the extent of success of the scheme which sacrificed considerable revenue for the sake of earning additional foreign exchange, an appraisal of the GJUs set up under the EPZ/the EOU scheme was carried out in some of the units located in the EPZs at Noida, Santa Cruz, Madras, Cochin and of the SEOC at Jhandewalan (New Delhi) during November 1995 to September 1996. Records maintained by the concerned Development Commissioners and the Customs department were test checked to determine:

- (i) whether the GJUs availing the duty exemption had fulfilled the prescribed pre and post importation conditions,
- (ii) whether foreign exchange for the declared value of exports have been realised,
- (iii) whether duty was collected in time in cases of violation of the conditions in exemption notifications and the Exim Policy,
- (iv) whether monitoring was adequate,
- (v) whether the scheme as a whole suffered from any lacuna.

### 3.3 Highlights

**The appraisal highlights the following points:-**

- i) Out of 80 units test checked, 41 units failed to achieve the prescribed value addition. Pro rata customs duty recoverable in these cases worked out to Rs.157.72 crores**

[Para 3.4]

- ii) 11 units could not account for 121 Kgs. of gold received by them from MMTC, for which customs duty amounting to Rs.4.78 crores was recoverable.**

[Para 3.5]

- iii) Dichotomy and contradiction in the scheme have given rise to doubts regarding the liability for payment of customs duty in the event of non-fulfilment of the export obligation.**

[Para 3.6.1 & 3.6.2]

- iv) Over-lapping responsibility and jurisdiction facilitated abuse of the scheme. Successful implementation of the scheme required constant**

**co-ordination between the Development Commissioner, MMTC and Customs authorities, which was found to be grossly inadequate.**

**[Para 3.6.5]**

- v) **None of the concerned agencies were adequately monitoring the fulfilment of export obligation by the GJU's. No verification was being done by MMTC to check utilisation of the gold already released before issue of further quantities. Laxity on periodic checks of the records/stock of the gold in the units by Customs authorities was noticed.**

**[Para 3.6.6]**

- vi) **Export obligation was taken as fulfilled on the basis of trading records (i.e. shipping documents), while records of the RBI showed that foreign exchange amounting to Rs.57.65 crores remained unrealised in respect of 30 GJUs in SEEPZ and Noida.**

**[Para 3.7]**

#### **3.4.1 Shortfall in value addition**

In terms of the Exim Policy 1992-97, the GJUs under the EOU/EPZ Schemes are required to attain a minimum value addition of 10 per cent for plain gold jewellery and 15 per cent for studded gold jewellery, failing which the pro-rata customs duty forgone on the corresponding imports alongwith penalty is recoverable. The formula of value addition has been discussed in para 2.1 supra.

Test check of the records of 80 units in Santa Cruz, Madras, Cochin, and Noida EPZs and Jhandewalan SEOC revealed that 41 units had failed to achieve the required value addition. The customs duty recoverable in respect of imports made by the defaulting units within Noida EPZ between 1992-93 to 1995-96 worked out to Rs.94.90 crores. In respect of the EPZs at Santa Cruz, Madras and Cochin, the duty recoverable in respect of imports between 1990-91 to 1995-96 added up to Rs.24.32 crores. In respect of SEOC, Jhandewalan, the duty recoverable in respect of imports between 1988 and 1994 worked out to Rs.38.50 crores. Audit findings in respect of the above are briefly narrated hereunder:

#### **3.4.2 Noida EPZ**

The 40 units in Noida received a total quantity of 6566 Kgs. of gold from MMTC on loan basis during the period 1991-92 to 1995-96. This constituted approximately 80 per cent of the total quantity of gold procured by these units, the balance 20 per cent being imported directly. Out of these 40 units, 26 failed to achieve the prescribed value addition and fulfil the export obligation.

The pro-rata duty corresponding to the shortfall in exports in respect of 17 units, which were found to have been closed down, worked out to Rs.33.13 crores. Out of the 23 working units, 9 failed to fulfil their export obligation, for which the prorata duty recoverable was found to be Rs.61.77 crores. Thus the total duty recoverable works out to Rs.94.90 crores. Since separate accounts showing the quantity and value of exports relating to (i) gold received from MMTC on loan and (ii) direct imports were not being maintained by these units, the exact liability of MMTC could not be worked out. Customs authorities were also unable to furnish the required break-up. However, as approximately 80 per cent of the total gold was supplied by MMTC on loan, liability of MMTC on pro-rata basis worked out to Rs.76 crores. No information regarding the action taken by the Customs authorities to recover the aforesaid amount has been made available to Audit. Action taken by the Development Commissioner against the defaulting units was also not made available to audit.

### 3.4.3 Jhandewalan SEOC

On the basis of records made available, it was found that out of 9 units in Jhandewalan, 4 had defaulted in fulfilling their export obligation before closing down. Records regarding one more closed unit and the other functioning units were not available to ascertain the fulfilment of export obligation.

Records show that the four closed units obtained a total quantity of 1059 Kgs. of gold on loan from MMTC between 1988 to 1994. It was estimated that the duty exemption availed in respect of the aforesaid quantity of gold was Rs.38.50 crores. Thus, on account of their failure to achieve the export obligation, the duty recoverable from the four units works out to Rs.38.50 crores. Further, in terms of the LUTs executed by the units with the Development Commissioner, 18 per cent interest on the duty recoverable was also chargeable. No action to recover either the duty or the interest was reported as of December 1996.

### 3.4.4 Other EPZs

11 other GJUs working for more than 5 years in SEEPZ, MEPZ and CEPZ failed to achieve the required value addition. The prorata duty corresponding to the shortfall in value addition worked out to Rs.24.32 crores as shown below:

EPZ	No. of units	period	Duty forgone on imported goods corresponding to the shortfall (Rupees in lakhs)
SEEPZ	7	1990-91 to 1994-95	1584.30
MEPZ	3	1989-90 to 1995-96	825.52
CEPZ	1	1990-91 to 1994-95	*22.14
Total	11		2431.96

\*Only for capital goods

### 3.5 Unaccounted for gold

In terms of condition 9 of Notification No. 177/94-Cus., in the event of a unit ceasing to operate, closing stock of gold, other precious metals, alloys, gem and other materials are to be handed over to an agency nominated by the Ministry of Commerce. At Noida EPZ, out of the aforementioned 17 closed units, 11 units could not account for 121 Kgs. of gold (valued at Rs.4.72 crores) received by them from MMTC between 1988 and 1995. The duty recoverable by the department from MMTC on this account worked out to Rs.4.78 crores. The interest amounting to Rs.1.8 crores is also recoverable from the units in terms of the LUT by the concerned Development Commissioner. These units are further liable to pay a penalty under the provisions of the REP circular No.22/88 at the rate of 10 per cent of the value of gold, besides penalty under the provisions of FTDRA. No action to recover either the duty or the interest has been reported as of December 1996.

The extent of irregularity/malpractice involved in the utilisation of gold in respect of some of these cases are narrated below.

3.5.1 One unit started production in May 1992 but closed down in April 1994. On being informed by MMTC on 24 March 1995 that the unit had not given the account of 7 Kgs. of gold valued at Rs.27.50 lakhs received by it between June to September 1993, the Assistant Commissioner of Customs conducted a search of its premises on 18 May 1995 and found 7.5 Kgs. of **'gold plated silver jewellery'**.

Duty forgone on 7 Kgs. of gold amounted to Rs.31.01 lakhs which was recoverable alongwith an interest of Rs.12.37 lakhs. A show cause notice had been issued on 20 March 1996 by the DGFT. Further progress was awaited (August 1996).

3.5.2 A unit commenced its production in May 1993 but closed down in March 1994. It received 45 Kgs. of gold from MMTC and exported 33 Kgs. of gold jewellery. Thus 12 Kgs. of gold valued at Rs.46.78 lakhs remained unaccounted. MMTC was issuing gold to the unit regularly without verifying the availability of stock. It was noticed that the gold usually retained by the unit exceeded the permissible limit of 10 Kgs. as fixed by the Development Commissioner. Moreover, it was found that the unit achieved a negative value addition(-19%).

The Development Commissioner and the Customs authorities came to know of the closure of the unit only in January 1995 when MMTC intimated that the unit had defrauded them of Rs.1.2 crores by way of non realisation of export proceeds. The Customs authorities also found that 12 Kgs. of gold was clandestinely removed from the bonded area and was able to seize only 10.35 Kgs. of **'gold plated silver jewellery'** from the strong room of the unit on 9 February 1995.

Duty forgone amounting to Rs.50.90 lakhs along with interest of Rs.16.93 lakhs was recoverable from the unit. DGFT issued a show cause notice on 16 April 1996 for levy of penalty for non achievement of value addition and export obligation. Further progress of the case was awaited (August 1996).

3.5.3 One unit obtained 65 Kgs. of gold on loan from MMTC against which it exported 49 Kgs. of jewellery during 1993-94 to 1995-96. Although the last consignment of export was on 3 July 1995, gold was still being regularly given to the unit upto December 1995 without any verification regarding the utilisation of the precious metal already issued.

On 30 April 1996, it was found by the Customs authorities that the assessee had **absconded** with 16 Kgs. of gold, valued at Rs.67.20 lakhs. The duty forgone in respect of 16 Kgs. of gold amounted to Rs.70.73 lakhs. An SCN had been issued by DGFT in June 1996 for levy of penalty but is yet to be adjudicated (August 1996). No action to recover the duty has been reported as of December 1996.

3.5.4 A unit which started functioning from 31 December 1991, was closed down in June 1995, without fulfilling the export obligation. In spite of this failure, the Development Commissioner recommended to MMTC for issue of further gold to this unit. As a result, 12 Kgs. of gold, valued at Rs.48 lakhs was obtained by the unit between April 1995 and June 1995 before its closure. In February 1996 the Development Commissioner, on physical verification found 'nil' stock of gold. Although duty forgone amounted to Rs.34.80 lakhs and interest chargeable to Rs.2.32 lakhs, no action for recovery had been reported as of December 1996.

### 3.6 Supply of gold by MMTC

3.6.1 The cases discussed in the foregoing paragraphs reveal that implementation of the scheme did not rest with a single nodal agency. Various agencies entrusted with overseeing/implementing different aspects of the scheme needed excellent co-ordination amongst them which was found lacking. This lack of coordination arose from the dichotomy and contradiction in the scheme itself. While the two Customs notifications No 3/88 and 177/94 envisaged that MMTC would be importing the gold as an agent of the GJUs and that all the necessary conditions were to be fulfilled by the concerned GJUs, REP circular of the Ministry of Commerce clearly defined the role of MMTC as the principal importer having full title to the imported gold which could be issued either on loan or on outright sale basis. The question of outright sale which involved transfer of title would not have arisen, had MMTC been importing gold only as an agent "on behalf of the jewellery units". The REP circular, further provided that, where the recipient unit failed to export the jewellery within the prescribed period, it was, obliged to

return the gold to MMTC with a penalty. All these indicate that MMTC was the focal point responsible for proper implementation of the scheme, timely discharge of the export obligation and levy of penalty in the event of delay/ shortfall in exports. But the Customs notifications clearly indicated that GJUs would execute a bond to pay customs duty forgone in respect of the gold received by them through MMTC, in the event of default. It was however, found that till early 1996 no such bond was being executed by the GJUs. Upon execution of the bonds, Customs authorities were empowered to recover duty from the defaulting GJUs who did not fulfil their export obligations but the Development Commissioners and not the Customs authorities remained responsible for ensuring fulfilment of such export obligations. It is, therefore, evident that for recovery of duty from the defaulting GJUs, the customs authorities had to depend on the Development Commissioners and any lack of coordination between these two authorities would result in defeating the very purpose for which duty exemptions were granted. It may be mentioned that audit did not come across any provisions in the Exim Policy or any executive instructions under which the Development Commissioners were obliged to furnish information regarding defaulting GJUs to the Customs authorities for further necessary action.

3.6.2 These anomalies and contradictions between the provisions of the customs notification (which is the sole authority for grant of any exemption/recovery of customs duty) and the said REP circular of the Commerce Ministry have given rise to doubts regarding the liability for payment of customs duty in the event of non-fulfilment of the export obligation. Although the customs notification envisaged import of gold by MMTC "on behalf of the jewellery units", in practice, the gold was imported by MMTC in bulk and at the point of importation, a bond was executed with the custom authorities by MMTC. The names of GJUs could not be mentioned in this bond for obvious reasons. Having executed the bonds, however, MMTC has not honoured the demand notices issued by the Customs authorities for recovery of the duty in the few cases of default brought to their notice. **In June 1996, MMTC disowned any liability for payment of customs duty for non-fulfilment of export obligation by the GJUs. Such a claim is evidently not a valid one in the face of the bond executed by them with the Customs authorities.**

3.6.3 The gold given by MMTC on loan basis was without any collateral security. Only from February 1996, a system of graded bank guarantees ranging from 10 per cent to 100 per cent of the cif value of gold, depending on the age and performance of the units, was introduced. How far such a system covering part value of gold issued by MMTC will be effective in checking misuse/abuse of the scheme remains questionable.

3.6.4 While MMTC did not obtain any security for issue of gold on loan basis till February 1996, they remained liable (in terms of the bond executed by them) to pay the customs duty for the default of the GJUs over which they had nominal control. This arrangement was vulnerable on two counts;

- a) There was a risk of non recovery of the value of the gold loaned to the GJUs,
- b) MMTC was liable to pay the customs duty for non fulfilment of export obligation by the GJUs over which they had little control.

3.6.5 Another aspect which needs to be elaborated is the system of divided as well as overlapping responsibility and jurisdiction which facilitated abuse of the scheme. While the Development Commissioner was responsible for monitoring the fulfilment of the export obligation and was accepting a separate LUT from the GJUs, MMTC was also responsible for ensuring discharge of the export obligation in respect of the gold released by them. Customs authorities, on the other hand, were responsible for ensuring proper maintenance of the records, periodic verification thereof and periodic check of stock etc., to ensure proper utilization of the duty free gold. Successful implementation of the scheme, thus, required constant co-ordination between the Development Commissioner, MMTC and Customs authorities, which was found to be grossly inadequate. Even when the irregularities came to light, there was further delay in initiation of penal action against the defaulting units. As a result, barring a few cases, no penalties were found to have been imposed on the defaulting units in the cases test checked.

3.6.6 No verification was also being done either by the Development Commissioner or by the MMTC or by the Customs authorities to check the utilisation of the gold already obtained by the units on loan basis before issue of further quantities. It was also seen that the Customs authorities did not carry out periodic checks of the records/stock of gold in the units.

### 3.7 Non realisation of foreign-exchange

As per the formula given in para 119 of the Exim Policy 1992-97, the value addition was to be calculated on the basis of fob value of exports **realised** but it has come to notice that the Development Commissioners were relying on the value declared on the shipping bills for discharge of export obligation and value addition. This practice of relying on the trading records instead of the payment records was faulty, as it has come to notice from the records of the RBI that a total fob amount of Rs.47.97 crores remained outstanding for more than six months in respect of 11 units of Santa Cruz Zone as of December 1995 and another Rs.3.48 crores was outstanding in respect of 4 other units of the same



zone as of June 1996. A total fob amount of Rs.6.20 crores realisable by 15 units in Noida also remained outstanding for more than six months as of July 1996.

Apart from defeating the very purpose of earning additional foreign exchange, such non realisation also violated the provisions of FERA which requires repatriation of proceeds within 6 months from the date of export. But the concerned departments have failed to monitor this aspect or to report the matter to the DGFT who is empowered to initiate necessary penal action. The abuse of the scheme is, further, emphasised by the finding that, in 3 out of the above 15 cases relating to Noida, the consignees mentioned in the shipping bills were related to the consignors.

### **3.8 Non-maintenance of records**

3.8.1 Relevant Customs notification provides that the importer shall maintain a proper account of the import, consumption and utilisation of the imported materials.

(i) At Noida EPZ, none of the units test checked were maintaining the records relating to the wastage of gold arising in the course of manufacture of jewellery. Twelve units manufacturing plain/studded jewellery had claimed a total wastage of 70.6 Kgs. valued at Rs.2.65 crores. The duty forgone on this quantity amounted to Rs.2.78 crores. None of the other units claimed any wastages. The department does not appear to have analysed the reasons as to why some of the units had claimed wastages while others did not.

ii) It was further observed in NEPZ, that neither the Development Commissioner nor the concerned Assistant Commissioner (Customs) was maintaining proper account of the quantity of gold received by the units, amount of duty forgone thereon and the exports of manufactured jewellery made out of such gold. The MMTC was maintaining only the account of the gold given to the units on loan/outright sale basis. Since MMTC was liable to pay the customs duty for the default of the GJUs, they should have evolved an effective system to monitor the performance of the GJUs.

3.8.2 Test check of the Bonds/the Bond Register available with the department in NEPZ revealed the following irregularities/deficiencies:

- a) Many bonds furnished by the units were found blank in regard to value of goods, amount of duty, period of validity etc.,
- b) No columns for noting the quantity/weight of raw materials were provided in the register,
- c) Cuttings, erasings and overwritings were not attested by any responsible authority in most cases,

- d) Entries in the register were not attested in most cases,
- e) Validity period of bonds were not noted in most cases.

3.8.3 While conducting a stock verification (December 1995) of the gold at 46 units in SEEPZ, the department noticed a shortage of 214.45 Kgs. in 43 units on account of availment of higher wastages. Show cause notices were found to have been issued to 40 units in April 1996 for recovery of customs duty amounting to Rs.5.12 crores. No reason for not issuing notices to the remaining three units for shortage of 5 Kgs. gold, involving duty exemption of Rs.14.28 lakhs, had been recorded. Further progress in the matter is awaited (December 1996).

No records were maintained by four units in SEEPZ to indicate the utilisation of the materials imported duty free in 1993-94. Action taken by the Department in these cases is also awaited (December 1996).

3.8.4 Three GJU's in Madras EPZ who did not maintain any accounts showing the wastage arising in the manufacturing process, claimed 9.941 Kgs. of gold valued at Rs.34.23 lakhs as wastages since their inception to the end of March 1996. The duty involved worked out to Rs.40.12 lakhs.

The facts were brought to the notice of the Development Commissioner, MEPZ and the Assistant Commissioner of Customs, Madras (July 1996). Their reply is awaited as of December 1996.

3.8.5 MMTC has been accepting bank guarantees since February 1996 from the working units. The details of these bank guarantees are noted in a register maintained for the purpose. However no proper format for the register has been prescribed. A scrutiny of the bank guarantee register revealed the following deficiencies:

- a) Neither the weight nor the value of the gold supplied on loan to the units was noted in the register. No column was provided to facilitate cross checking whether the bank guarantees covered the value of gold. Out of 26 entries made in the register, 12 entries were found to have been cancelled subsequently without proper attestation by any responsible officer.
- b) The bank guarantees were being taken on the basis of a notional price of gold declared by the MMTC, which were at variance with the domestic price of gold prevailing on the date of the transaction.

3.9 The above points were brought to the notice of the Finance Ministry and the Ministry of Commerce in November 1996. Their replies have not been received (December 1996).

#### 4. SHORT LEVY DUE TO UNDERVALUATION

Some of the illustrative cases of underassessment of duty, which came to light during test audit, are narrated below:

##### 4.1 Non adoption of price variation

A PSU exporting iron ore to Japan received additional payments arising from upward revision of the price of iron ore exported between March 1992 to July 1992. It was seen in course of Audit in December 1994 that the additional price was not taken into account while arriving at the value for the purpose of assessment of the export duty on the goods. The adoption of incorrect assessable value resulted in short collection of export duty amounting to Rs.14.14 lakhs.

The department recovered the duty short levied in October 1995.

##### 4.2 Incorrect grant of depreciation

a) The Ministry in a circular issued on 19th November 1987 laid down that the maximum depreciation which could be allowed for valuation of imported second hand machinery was 70 per cent. In terms of this circular, the assessable value of an 'Automatic test system' manufactured in 1980 and imported by a PSU in September 1994 worked out to Rs.11.27 lakhs after allowing the maximum depreciation of 70 per cent, as against the amount of Rs.3.33 lakhs adopted by the department. The undervaluation and consequent short levy of duty amounting to Rs.2.98 lakhs was pointed out to the department (November 1995). The department accepted the audit observation in May 1996. Recovery particulars are awaited (October 1996).

b) A 'Toyota sera' car was imported by an individual in August 1993 declaring its value as Rs.1.50 lakhs. The department, after due investigations, concluded that the importer had attempted to claim ineligible depreciation by giving false information about the date of registration. Accordingly, in the adjudication order dated 6 January 1994, the claim for depreciation on car was disallowed and the value of the car was determined at Rs.4.77 lakhs. The importer was given an option to redeem the car on payment of a fine of Rs.3 lakhs and penalty of Rs.50,000. An appeal by the importer was also rejected on 28 March 1994 by the Appellate authority, who upheld the original order stating that the appellant did not satisfy the conditions regarding the use and possession of the car and that the appellant was not eligible for benefit of any depreciation.

It was, however, noticed that in disregard of the orders passed by the Appellate Authority, depreciation was allowed and the car was released in June 1994 after collecting Rs.5.21 lakhs as duty. As the duty on the assessable value of

Rs.4.77 lakhs worked out to Rs.7.60 lakhs, the short levy of duty of Rs.2.39 lakhs was pointed out to the department in July 1995.

The department contended in February 1996 that the duty was correctly worked out after allowing a depreciation of 35.5 per cent. The depreciation allowed by the department in June 1994 was inconsistent with their earlier conclusion, subsequently upheld by the Appellate Authority, that no depreciation should be allowed under the facts and circumstances of this case.

The matter was referred to the Ministry in July 1996; their reply was awaited as of October 1996.

#### 4.3 Non adoption of sale price on high seas

According to rule 3(1) of the Valuation Rules, the value of imported goods shall be the transaction value, which, in case of goods sold on high seas, is the actual sale price and includes expenses such as commission charges incurred by the importer.

a) 'Metallurgical grade silicon' and 'Polypropylene homopolymer' imported by three private importers and sold on high seas were assessed to customs duty on the actual invoice value without taking into account the service charges, such as banker's charges/licence premium/commission etc. resulting in short collection of duty to the extent of Rs.1.09 lakhs.

The department accepted (December 1995) the audit objections raised during December 1990 to April 1992 but recovery particulars are awaited.

b) In case of another import (August 1990) canalising charge was not considered for determination of assessable value of the goods, though it was realised by the canalising agency in addition to the transaction value of the goods for sale on high seas. This resulted in short collection of duty of Rs.1.14 lakhs.

The department admitted (November 1995) the objection but report of recovery was awaited as of July 1996.

c) In the case of an importer 'A', selling imported 'Metal scrap' to Indian buyers on high seas, the department computed the value on the basis of the invoice raised by the foreign seller against the importer 'A'. It was pointed out that the duty should have been assessed on the basis of invoices raised by importer 'A' against the Indian buyers.

The incorrect computation of assessable value resulted in short levy of duty amounting to Rs.5.97 lakhs. Although this was pointed out in August 1993, the department's reply was awaited as of October 1996.

#### 4.4 Incorrect computation of assessable value

In terms of Rule 9(1) (e) read with Rules 3(i) and 4 of the Valuation Rules, all payments made as a condition of sale of the imported goods by the buyer to the seller, or by the buyer to a third party to satisfy an obligation of the seller shall be included in the transaction value of the imported goods for the purpose of assessment of customs duty, provided that such payments are not included in the price actually paid or payable.

In respect of a consignment consisting of 'Canned centrifugal pumps and spares' imported (October 1989) by a Government of India undertaking, 'expediting fee of JY 20,00,000 for 90 days delivery' was not included in the transaction value. The said fees, being a condition of sale were to be included in the assessable value. The non inclusion of such fees resulted in undervaluation of the imported goods and consequent short collection of duty of Rs.3.45 lakhs which was pointed out in April 1990.

The department contended that the expediting fees was a financial arrangement similar to interest for deferred payment and did not fall in the category of pre-importation liability and that such charges were excluded from the assessable value as per Interpretative notes to Rule 4.

The department's reply is not tenable for the following reasons:

- i) the expediting fees paid cannot be compared with interest for deferred payment, since the former is meant for obtaining delivery within a specified time while the latter enables the buyer to pay in a staggered manner. Expediting fees is also not a financial arrangement but only an option exercised by the buyer for ensuring quicker delivery.
- ii) Interpretative notes to Rule 4 cannot be applied as the said notes specifically excludes all adjustments contemplated under Rule 9 *ibid*.

The matter was referred to the Ministry in August 1996; their reply was awaited as of October 1996

#### 4.5 Incorrect mode of computation of value for levy of additional duty

Where additional duty of customs is leviable as any percentage of the value of goods, the value of the imported article as per Section 3(2) to the Tariff Act, shall, notwithstanding the provisions of Section 14 of the Act, be the aggregate of;

- i) the value of the imported article determined under Section 14 of the Act, or the Tariff value fixed under sub-section (2) of that section, as the case may be.
- ii) any duty of customs chargeable on that article under Section 12 of the Act.

A consignment of 'Polyester monofilament yarn type 264 - Semi dull round' imported during June 1995 was charged to additional duty of customs at the rate of 50 per cent of the tariff value of Rs.90 per Kgs. fixed under Section 3 of the Central Excises Act, 1944 with Cess at 0.05 per cent, as against 50 per cent of the value to be adopted under Section 3 (2) of the Tariff Act. The incorrect mode of computation of additional duty resulted in short levy of Rs.0.95 lakh.

The department's reply to the audit objection issued in March 1996 was awaited as of October 1996.

#### **4.6 Adoption of incorrect rates of exchange**

As per proviso to Section 14(1) of the Act, the rate of exchange for conversion of value expressed in foreign currency in respect of any imported goods is the rate in force on the date of presentation of the bill of entry.

In a major Custom House, incorrect rates of exchange were adopted in respect of 14 consignments of dutiable goods imported during March 1995, resulting in short levy of Rs.13.55 lakhs. When the cases were referred to the department during July 1995 to January 1996, the department admitted the errors in all cases and reported recovery of Rs.10.03 lakhs, relating to 12 cases during August 1995 to March 1996.

### **5. SHORT LEVY OF DUTY DUE TO INCORRECT CLASSIFICATION**

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

#### **5.1 Machineries/parts**

##### **a) Fuel pump elements**

A consignment of 'Fuel pump elements' intended for use in the Fuel Injection Pumps was classified under sub heading 8409.99 of the Tariff as "Parts of Internal Combustion Piston Engine" (September 1992) instead of as "Parts of Fuel Injection Pumps" under heading 8413. The misclassification and the incorrect application of exemption notification covering goods falling under heading 8409, resulted in short levy of Rs.4.40 lakhs.

The Ministry have admitted the objection in August 1996 but the details of recovery are awaited as of December 1996.

##### **b) Weaving machines**

'Weaving machines' are classifiable under sub heading 8446.29 of the Tariff for the purpose of levy of basic customs duty and under sub heading 8446.00 of the Central Excise Tariff for levy of additional duty of customs. A

consignment of 'Dornier rapier weaving machine', imported during February 1994, was classified under sub heading 8448.49 of both the Tariffs as 'Machines for drawing, extruding, texturing or cutting man made textile materials'. When the mistake in classification which resulted in short levy of Rs.12.20 lakhs, was pointed out in audit (July 1994), the department accepted (March 1995) the classification under heading 84.46 but stated that there was no short levy as the goods were exempt under serial No.18 of notification No.21/88-Cus.

The reply is not tenable as the notification allowed concessional rate of duty, among other items, to "Automatic looms used in woolen industry for weaving plain plush and jacquard plush fabric" and not to 'Dornier rapier weaving machine'.

The Ministry's reply is awaited as of October 1996.

**c) Risograph printers**

Five consignments of 'Risograph printers with drums and stands' imported between May and September 1994 were classified under sub heading 8443.50 of the Tariff covering 'Printing machinery'. The 'Risograph printer', being a kind of Duplicating machine, was classifiable under heading 8472 as 'Office machines'. The incorrect classification resulted in short levy of Rs.21.91 lakhs. On this being pointed out in December 1994, the department accepted the objection and effected recovery (June 1995).

**d) Thrust pads for gearings**

One consignment of 'Thrust pads made of Babbitt material with Steel back' for use in 'Thrust bearing assembly', imported in March 1993, was classifiable under sub heading 8483.90 as 'Parts of shaft bearing assembly'. Such machinery was classifiable under sub heading 8406.90 as 'Parts of turbine'. The incorrect classification resulted in a short levy of Rs.6.20 lakhs. This was pointed out in August 1993.

The Ministry have confirmed the facts (September 1996), but recovery particulars are awaited as of October 1996.

**5.2 Electrical/electronic goods, parts**

**Tungsten electrodes**

3 consignments of imported 'Niobium supports' and 'Tungsten electrodes' - (parts of High pressure sodium vapour lamps) - were respectively classified and assessed under sub headings 8102.99 and 8101.99 of the Tariff as 'Articles of niobium and tungsten'. Being parts of Electric Lamps, the goods were correctly classifiable under sub heading 8539.90 of the Tariff. The mistake in classification

resulted in a short levy of Rs.3.62 lakhs. The department did not accept the objection and stated that the imported goods had to undergo processing before becoming part of a lamp. Two High Court decisions in favour of classification as 'Tungsten electrodes' under heading 81.09 were cited in support of the assessment under chapter 81.

The department's contention could not be accepted due to the following reasons:-

- i) As per section 2(a) of the Interpretative Rules of the Tariff, any reference in a heading to an article shall be taken to include a reference to that article incomplete or unfinished, provided that the incomplete or unfinished article has the essential character of the complete or finished article. It shall also be taken to include a reference to that article complete or finished in un-assembled or disassembled forms. The impugned goods had the identity of a part of electric lamp and was described in the bills of entry as such.
- ii) The decisions relied on by the department were with reference to the pre-revised Tariff in which a specific sub heading for 'Parts' of Electric Lamps was not available under Tariff heading 8539.
- iii) In subsequent imports the department classified Tungsten electrodes under sub heading 8539.90 as was pointed out by audit in the instant case.

The Ministry has accepted the view of Audit in December 1996.

### 5.3 Motor vehicles

#### Mobile concrete mixer

A consignment consisting of 'Highway mobile concrete mixer' imported during November 1995, was assessed under sub heading 8474.31 of the Tariff and sub heading 8774.10 of the Central Excise Tariff as 'Concrete mixing machine'. However, in terms of Explanatory Notes to HSN Volume 3 (page 1307) 'Concrete mixer lorries' permanently mounted on a lorry chassis and capable of being used for both mixing and transporting concrete, are excluded from the scope of chapter 84.74 and are classifiable under sub heading 8705.40 of the Tariff. For the purpose of levy of additional duty of customs, these items are classifiable under sub heading 8705.00 of the Central Excise Tariff.

The mistake in classification resulted in short levy of Rs.9.76 lakhs. It was pointed out in March 1996 but the Ministry's reply is awaited as of October 1996.



**5.4 Measuring, testing, checking instruments****a) Endoscope for automobiles**

A consignment of 'Endoscope inspection set' meant for checking Automobile components was classified (August 1994) under heading 9018, as a 'Medical equipment' instead of under sub heading 9031.80. The misclassification resulted in a short levy of Rs.1.74 lakhs.

The Ministry have confirmed the facts in August 1996 and reported recovery.

**b) Detection equipments**

'Pinhole tester and equipments', imported in January 1993 was classified and assessed to duty under sub heading 9024.80 covering 'Machines and appliances for testing the Mechanical properties of materials'. It was pointed out in audit (April 1993) that the goods were photo electric devices meant for detecting extremely small holes and other defects in moving sheets of material, and as such were correctly classifiable under sub heading 9031.80 as 'Other instruments, appliances, and machines not mentioned elsewhere in Chapter 90'. The incorrect assessment resulted in a short levy of Rs.3.25 lakhs.

The department accepted the objection in February 1996. But recovery particulars are awaited as of October 1996.

**5.5 Plastics****a) Cellulose acetate waste**

Three consignments of 'Cellulose acetate cuttings' imported during September and November 1990 were classified and assessed to duty under heading 39.20 as 'Plates/sheets of plastics'. As per the examination reports, the goods were 'Plastic scraps' and merited classification under heading 39.15. The incorrect classification resulted in a short levy of Rs.4.05 lakhs. Though the audit objections (January to July 1991) have been admitted by the department in January 1996, particulars of recovery are awaited as of October 1996.

**b) Polyvinyl pyrrolidone**

Goods described as 'Polyvinyl pyrrolidone K 30' was imported in February 1992 and assessed to duty under heading 29.42 as 'Organic compounds'. As per HSN, 'Polyvinyl pyrrolidone' is a Vinyl polymer classifiable under heading 39.05. The misclassification resulted in short collection of duty of Rs.5.76 lakhs. On this being pointed out in June 1992 the department admitted the objection in May 1996. Recovery particulars are, however, awaited as of October 1996.

## 5.6 Lubricating preparations

### Waste lubricating oil

A consignment of 'Waste lubricating oil' containing less than 70 per cent by weight of oil content, imported in March 1994, was assessed under Tariff heading 2710, covering 'Preparations containing 70 per cent or more of petroleum oils'. But the test report recorded on the bill of entry showed that the goods contained only 67 to 69 per cent by weight of oil content. The goods were therefore assessable under heading 3403.19. The incorrect classification resulted in a short levy of Rs.3.62 lakhs and was pointed out by audit in October 1995.

The department contended (December 1995) that the goods being 'Waste mineral oil' was not a preparation meant for lubricating purpose and hence could not be considered for classification under sub heading 3403.19. But a Tariff Advice issued on 11 January 1991 by the Collectorate based on Collectors' conference decision of October 1990 stated that 'Waste oil containing less than 70 per cent by weight of mineral oil' content would be classifiable under sub heading 3403.19, as the waste oils were generally refined and recycled as lubricating preparations.

Reply of the Ministry is awaited (October 1996).

## 5.7 Other cases

Some of the other cases of incorrect classification detected during test audit are mentioned in the table below:

(Rupees in lakhs)

Sl. No.	Details of product	Heading where classifiable	Heading where classified	Amount short levied	Amount accepted	Amount recovered
1.	Working tables for printing machines	94.03	8443.90	4.72	—	—
2.	Triaryl phosphate	34.03	27.10	6.19	6.19	6.19
3.	Tropical airconditioners	84.15	8525.10	8.82	—	—
4.	Precision balance of sensitivity more than 5 cg.	84.23	90.16	1.13	1.13	1.13
5.	Parts of machinery made of glass	70.20	84.19	0.92	0.92	0.92
6.	Mounting hubs; Transmission parts	8483.90	8431.49	1.11	1.11	1.11
7.	Springs of steel	73.20	84.48	1.53	1.53	1.53
8.	Governor gear assembly	8483.40	8409.99	0.71	0.71	—
9.	Articles of vulcanised rubber-airrides	4016.95	8439.90	2.01	2.01	2.01
10.	Sign plates of base metal	8310	76.16	0.84	0.84	0.84
11.	Magnetic tape drives	8471	8473	1.59	1.59	—
12.	Cannula needles	9033	9018	0.95	0.95	—
13.	Elpex coupling parts	8483.90	8474.90	1.57	—	—
14.	Scanning micro probe	8548	9012.90	0.67	0.67	0.67
Total				32.76	17.65	14.40

## 6. SHORT LEVY DUE TO INCORRECT GRANT OF EXEMPTION

Some illustrative cases of short levy of duty on account of incorrect grant of exemption are narrated below:-

### 6.1 Non verification of end use

Notification No.166/76-Cus. as amended, read with other notifications in force during 1989 to 1992, prescribed that Phosphoric acid when imported from Morocco for the manufacture of fertilisers was exempt from duty in excess of 12 per cent ad valorem.

A PSU diverted a part of the Phosphoric Acid imported under the aforesaid notification to another unit (1990 and 1991) for pollution control. As the PSU was not entitled to the benefit of the aforesaid notification in respect of the quantity diverted (18.40 MT), a short levy of Rs.1.89 lakhs resulted. This was pointed out in audit (March 1992/June 1993). The department admitted the objection and reported recovery of Rs.7.99 lakhs.

The Ministry stated in May 1996 that the diversion would have been detected by them at the time of finalisation of the assessment which was provisional.

### 6.2 Double benefit of exemption notification

A consignment of 'Components of monopolar membrane electrolyser' imported during May 1993 was assessed to duty in terms of notifications No.155/86-Cus. and No.63/87-Cus. However, explanatory note to notification No.155/86-Cus. prohibits the availment of the benefit of any other notification except 59/87-Cus. and 296/90-Cus. in respect of goods eligible for the benefit of notification No.155/86-Cus.

Short levy of duty on account of the irregular grant of exemption amounting to Rs.77.54 lakhs was pointed out in October 1993.

The Ministry confirmed the facts and reported (July 1996) recovery of the short levied amount.

### 6.3 Import by research institutions

In terms of a clarification issued by the Ministry of Education, 'Cameras' were not eligible for exemption under notification No.70/81-Cus., except where these formed an integral part of any scientific/technical equipment required by a research institution. Availing the benefit of the aforesaid notification, no duty was levied on four 'SLR cameras' imported (July 1989) by a research organisation of the Government of India, although these did not form an integral part of any scientific/technical equipment.

The incorrect grant of exemption and the non levy of duty amounting to Rs.8.38 lakhs was pointed out by audit in January 1990. The department admitted the objection in June 1991.

The Ministry have also confirmed the facts (September 1996) but recovery particulars are awaited.

#### **6.4 Import by private hospitals**

In terms of notification No.64/88-Cus., hospital equipments certified by the DGHS as essential for use by specified category of charitable hospitals, are exempt from payment of all import duties.

Availing the benefit of the aforesaid notification, no duty was levied on two consignments of hospital equipments imported by two private hospitals (January 1991) although no certificate of essentiality was issued by DGHS. On the incorrect grant of exemption and consequential loss of revenue of Rs.23.95 lakhs being pointed out by audit, the department admitted the omission (February 1996). Details of recovery are awaited as of October 1996.

#### **6.5 Imports by leather industries**

(a) Notification No.267/89-Cus. prescribes a concessional rate of duty on specified goods imported for use in leather industry. A consignment of 'Steel snap fasteners' imported during June 1993 was given the benefit of the said notification without any evidence to show that the required conditions had been fulfilled. This resulted in a short levy of Rs.2.16 lakhs.

The department admitted (March 1996) the objection but the details of recovery was awaited as of October 1996.

(b) 'Automatic spraying machine' designed for use in the leather processing and finishing industry was eligible for concessional duty of 35 per cent ad valorem and exempt from auxiliary and additional duties in terms of notifications No.43/78-Cus. and 122/92-Cus.

Certain accessories viz., 'Conveyors, dryers and coolers' imported in September 1992, not eligible for the aforesaid exemption, were wrongly given the benefit of the two above mentioned notifications, alongwith the main machine i.e. 'Rotopress autospray machine'. It was pointed out by audit (February 1993) that the optional accessories should have been assessed on the basis of their individual value. The department admitted the audit view and stated in May 1996 that a demand notice for Rs.5 lakhs was issued to the importer as the amount of short collection could not be quantified due to non availability of individual value of accessories.

### 6.6 Import of copper cables

A consignment of 'Copper cables' meant for transmission of electrical power was assessed (February 1993) to duty at concessional rates, which were applicable to 'Electric cables made other than of Copper' and 'Telecommunication cables', in terms of notification No.193/92-Cus. and 69/86-CE.

On the incorrect grant of exemption and the resultant short levy of Rs.6.43 lakhs being pointed by audit (July 1993), the department reported recovery in February 1996.

### 6.7 Incorrect grant of exemption to 'Folley balloon catheters'

Notification No.65/88-Cus. as amended from time to time prescribed a concessional rate of 15 per cent ad valorem on 'Suction catheters'.

28 consignments of 'Folley balloon catheters', imported during July 1994 to February 1995, were given the benefit of the said notification under the product group, 'Suction catheters'. It was decided in the Collectors Conference of June 1984 that 'Folley balloon catheters' were functionally different from 'Suction catheters' and were recognised as two different class of products in the trade. A specific note stating that 'Suction catheters' shall not include 'Folley balloon catheters' was appended to the prevailing notification No.208/81-Cus. covering 'Suction catheters' till 2 June 1994. A similar note was inserted in notification No.65/88-Cus. in March 1995.

When the incorrect grant of exemption and the resultant short levy of duty of Rs.32.03 lakhs was pointed out (December 1994 to January 1996), the department justified the assessment on the ground that 'Folley balloon catheters' were covered under the term 'Suction catheters'- specified in the notification and that the exclusion clause in the said notification came into force after the imports were made. The facts were referred to the Ministry in June 1995, but the Ministry upheld, in October 1995, the stand taken by the department. However, the Ministry's reply is not tenable for the following reasons:

- i) 'Folley balloon catheters' was not included as a specific item in the list appearing in notification No.65/88-Cus.
- ii) It did not fall under the broad category of 'Suction catheters', since both have been considered functionally different at the Collectors' Conference referred above.
- iii) The explanation inserted in March 1995 under notification No.65/88 reaffirmed the fact that 'Folley balloon catheters' were not covered by the term 'Suction catheters'. Such explanation, being clarificatory in nature, has retrospective effect in terms of the decision of the CEGAT in 1995(61) ECR 158.

### 6.8 Incorrect grant of exemption to 'Flax tow'

Notification No.40/93-Cus. prior to its amendment on 1 March 1994, prescribed a concessional rate of duty on 'Flax fibre'. 'Flax tow' and certain other types of tows were brought within the purview of the said notification with effect from 1 March 1994.

Eight consignments of 'Regined flax type sanetow', imported through two Custom Houses between November 1993 and January 1994, were assessed to duty at the concessional rate in terms of the said notification.

The supplier's literature showed that the goods were 'Flax tows' and being different from Flax fibres, these did not fall within the scope of the said notification till its amendment on 1 March 1994.

The total short levy resulting from the incorrect grant of exemption amounted to Rs.45.76 lakhs which was pointed out by audit in March 1994. The department did not accept the audit's view and stated that the term 'Flax fibre' was a general description covering 'Flax tow' which refers to broken and tangled fibre and that 'Flax tows' were covered in the notification from the very beginning. It was also pointed out that the notification was amended only to make the issue clear and not to expand its scope.

The reply of the department is flawed because an amendment to a notification has only prospective effect. Further in terms of Supreme Court ruling in *Novopan India Ltd. v. Collector of Central Excise and Customs, Hyderabad 1994 (54) ECR (505) SC*, there is no need to interpret an exemption notification if the wordings were plain and clear. Since the original notification specified 'Flax', and other Fibres only and not any kind of 'tow' which were later included by an amendment, Flax tows did not clearly fall within the scope of the notification till its amendment.

### 6.9 Other cases

In 8 other cases the objections issued to the Ministry involved short levy of Rs.31.35 lakhs of which Rs.12.10 lakhs had been recovered as per details given below:-

(Rupees in lakhs)			
Sl.No.	Products on which exemption granted incorrectly	Amount of short levy	Amount recovered
i)	Shoe stiffner material	0.98	0.98
ii)	Glass frit for TV picture tubes	3.96	3.96
iii)	Telemetry equipments and spares	1.27	1.27
iv)	Instrument cooling fan	1.18	1.18

(Rupees in lakhs)			
Sl.No.	Products on which exemption granted incorrectly	Amount of short levy	Amount recovered
v)	Aluminium extruded sections	3.37	3.37
vi)	Dried grapes	3.47	1.34
vii)	Rotor shafts	0.89	—
viii)	Leak tester	16.23	—
Total		31.35	12.10

## 7. NON LEVY/SHORT LEVY OF ADDITIONAL DUTY

As per Section 3 of the Tariff Act, any article which is imported into India shall be liable to 'Additional duty' equal to the central excise duty for the time being leviable on a like article produced in India in addition to the duty levied under Section 2.

Some illustrative cases of non levy/short levy of additional duty noticed in course of test audit are narrated below:

### 7.1 Short levy of additional duty due to misclassification

#### a) Radio transmission/Receiver apparatus

(i) 'Radio pagers', being a kind of radio telephony receivers, are classifiable under sub heading 8527.39 of the Tariff for levy of the basic duty and under heading 85.27 of the Central Excise Tariff for levy of additional duty.

A consignment of 'Radio pagers', imported during March 1995, was classified under heading 85.28 as Television receiver apparatus. The misclassification resulted in a short levy of additional duty amounting to Rs.17.91 lakhs.

When the irregularity was pointed out (March 1996), the Ministry admitted the objections and reported recovery in May 1996.

(ii) Parts of 'Radio transmission apparatus' are classifiable under Central Excise Tariff heading 85.29 for levy of additional duty.

A consignment of 'Sub-assemblies and modules for the manufacture of radio transmission equipment' was classified (June 1994) under heading 85.25 of the said Tariff, treating the goods as complete transmission apparatus. The misclassification resulted in additional duty being levied short by Rs.6.21 lakhs.

The Ministry have confirmed the facts (July 1996) and reported recovery of the short levy.

**b) Silicon wafers**

“Silicon wafers, discs or similar forms” for use in electronics and classifiable under heading 38.18 of the Central Excise Tariff, as well as those which are extensively worked (diffused) and classifiable as semi conductor devices under heading 85.41 of the said Tariff were exempt from levy of additional duty in terms of notification No.83/87-Cus. The said exemption was however, withdrawn from 4 May 1993 in respect of semi-conductor devices.

Twenty one consignments of ‘Diffused silicon wafers’, classifiable under heading 85.41, were imported by a PSU during June 1993 to January 1994, and wrongly classified under heading 38.18 without levy of additional duty of Rs.31.89 lakhs.

On the mistake being pointed out (May/June 1996), the Ministry confirmed the facts (July/October 1996) and reported recovery in respect of all the consignments.

**c) Coated paper**

11 consignments of different kinds of ‘Coated/impregnated/covered/surface coloured/printed paper’, classifiable under sub heading 4811.90 of the Central Excise Tariff for the purpose of levy of additional duty, were imported/cleared from bonded warehouses during January 1992 to September 1993, after being incorrectly classified and charged to lower rates of additional duty. The total short levy as a result of this misclassification worked out to Rs.8.25 lakhs which was pointed out by audit during May 1992 to March 1994.

The department admitted the objections and reported recovery of an amount of Rs.4.75 lakhs in 3 cases. The Ministry have also confirmed the facts (May 1996).

**d) Gearbox couplings**

A consignment of ‘Gearbox, fluid couplings and its parts’, classifiable under sub heading 8483.40 and 8483.90 respectively, was imported during October 1995 but classified under Tariff sub heading 8430.69 for levy of basic and additional duties of customs. The misclassification resulted in short levy of additional duty of Rs.10.29 lakhs.

On this being pointed out in audit (March 1996), the Ministry admitted the objection in October 1996; however recovery particulars are awaited as of December 1996.



**7.2 Non levy/short levy of additional duty**

(i) Goods imported and assessed to basic duty in terms of notification 20/88-Cus., 65/88-Cus., 66/88-Cus. and 97/89-Cus. were exempt from additional duty in terms of the said notifications. The said exemption was, however, withdrawn with effect from 21 July 1993.

In case of six consignments of various dutiable goods imported through three major Custom Houses during July 1993 to December 1993, additional duty amounting to Rs.7.39 lakhs was not levied, although the relevant exemption had already been withdrawn.

The Ministry have confirmed the facts (August 1996) and reported recovery of Rs.5.22 lakhs in three cases.

(ii) Partial exemption from levy of additional duty was available in respect of Electric motors and generators (excluding generating sets) in terms of notification No.52/93-CE but the exemption was withdrawn with effect from 27 September 1993.

In a Custom House, Electric motors of various types imported on or after 27 September 1993 by seven importers, were classified under heading 85.01 of the Central Excise Tariff and assessed to additional duty at concessional rates applicable prior to 27 September 1993. This resulted in a short levy of Rs.4.70 lakhs.

The department accepted the audit objections (December 1995) and reported recovery of an amount of Rs.3.45 lakhs.

The Ministry's reply have not been received (October 1996).

**7.3 Short levy of additional duty due to application of incorrect rates**

Two consignments consisting of 'Spares for valves' and 'Glow plugs', imported during February/March 1995, were assessed to additional duty under sub headings 8481.90/8536.90 of the Central Excise Tariff at rates lower than those applicable. On the resultant short levy of additional duty amounting to Rs.3.92 lakhs being pointed out by audit (August 1995), the department accepted the objection and recovered the short levied duty in September/December 1995.

The Ministry have confirmed the facts (May 1996).

**7.4 Short levy due to incorrect grant of exemption**

In terms of notification No.33/90-Cus., goods falling under heading 25.30 of the Tariff were exempt from payment of additional duty but the said exemption was withdrawn with effect from 21 July 1993.

Two consignments of 'High grade manganese ore' (battery grade) were imported and cleared from a bonded warehouse on or after 21 July 1993 without charging the additional duty. This resulted in a short levy of Rs.2.34 lakhs.

When the facts were brought to the notice of the Ministry, it stated (May 1996) that the goods continued to be exempted by another Central Excise notification covering 'Natural mineral - manganese dioxide'. The reply is not tenable since 'Mineral manganese dioxide' is clearly distinguishable from 'High grade manganese ore' as a separate Tariff item.

### 7.5 Other cases

In 29 other cases, incorrect classification, wrong application of rates of duty, incorrect application of exemption notification, etc., resulted in a short levy of additional duty amounting to Rs.47.51 lakhs of which 24 cases involving Rs.39.94 lakhs had been accepted as per details below:

(Rupees in lakhs)					
Sl. No.	Item on which duty short levied	Irregularity	Amount short levied	Amount accepted	Amount recovered
1.	Poly propylene (3920.39)	Misclassification	1.00	1.00	1.00
2.	Digital TBC (85.43)	Misclassification	1.44	1.44	1.44
3.	Acrylic polymers (3906.90)	Misclassification	1.67	—	—
4.	Artificial waxes (34.04)	Misclassification	1.85	—	—
5.	Tyres for use in vehicles off the road (4011.91)	Misclassification	1.48	1.48	1.48
6.	Aeroplane tyres (4011.91)	Misclassification	2.83	1.38	1.38
7.	Medical equipments	Non levy of additional duty	0.80	0.80	0.80
8.	Non levy of duty on goods imported under qbal	Non levy of additional duty	1.07	1.07	1.07
9.	Articles for use in leather industry	Non levy of additional duty	1.11	1.11	1.11
10.	Spares for engines	Incorrect rates of additional duty	1.32	1.32	1.32
11.	Melamine	Incorrect rates of additional duty	2.06	2.06	2.06
12.	Sound deadening cabins	Incorrect rates of additional duty	1.33	1.33	1.33
13.	Valves and hoses	Incorrect rates of additional duty	1.78	1.78	1.78
14.	Electrical components	Incorrect rates of additional duty	2.71	2.71	2.71
15.	Components of autoclave Heating exchange	Incorrect rates of additional duty	2.24	2.24	2.24
16.	Parts of compressor for refrigeration	Incorrect rates of additional duty	1.33	1.33	1.33
17.	Mid finger conveyer chip soldering system	Incorrect rates of additional duty	1.07	1.07	1.07
18.	Catalyst	Incorrect rates of additional duty	1.72	1.72	1.72
19.	Floppy Diskettes	Incorrect rates of additional duty	2.07	2.07	—
20.	Graphite Electrodes	Incorrect rates of additional duty	1.90	1.90	—
21.	Components of hydraulic motors	Incorrect rates of additional duty	1.50	1.50	—

(Rupees in lakhs)

Sl. No.	Item on which duty short levied	Irregularity	Amount short levied	Amount accepted	Amount recovered
22.	Bareflat copper wire	Incorrect rates of customs duty	1.57	1.57	—
23.	Valve face regrinding machines	Incorrect rates of customs duty	2.60	—	
24.	Goods for leather Industry	Incorrect application of Exemption notification	1.51	1.51	1.51
25.	Man made fabrics	Incorrect application of Exemption notification	1.02	1.02	1.02
26.	Switches & connectors	Incorrect application of Exemption notification	1.60	1.60	1.60
27.	Precision balances	Incorrect application of Exemption notification	1.22	1.22	—
28.	Articles of polyurethene	Incorrect application of Exemption notification	1.94	1.94	—
29.	Viscose staple fibre	Non levy of additional duty	1.77	1.77	1.77
TOTAL			47.51	39.94	29.74

## 8. IRREGULARITIES IN DUTY EXEMPTION SCHEMES

Duty exemption is available to imports meant for manufacture of goods for exports under several export promotion schemes (other than those included in para 2 and 3) viz., VABAL, QABAL and EPCG. While these duty exemptions are regulated under notifications issued by the Board, the schemes are basically administered by the Ministry of Commerce. Some illustrative cases of irregularities noticed during test audit of records relating to imports under the three above mentioned schemes are narrated below:

### 8.1 Non recovery of duty

As per Exim Policy 1992-97, the regional licensing authority may grant a maximum extension of one year for fulfilment of export obligations, but any request for extension made after two months of the expiry of the initial export obligation period shall be summarily rejected.

Thirty-two advance licences were issued by the DGFT, during 1990 to 1992 to a company for the export of aluminium alloy, aluminium alloy ingots, solder wire, lead wire, lead alloy, boric acid etc. with a validity period of one year. The time limit for fulfilment of export obligation ranged from November 1992 to April 1993. Duty free inputs like aluminium dross/scrap, tin, lead scrap, silicon, nickle etc. involving duty exemption of Rs.45.73 crores were imported against these licences during 1990 to 1992. While there was no export within the original export obligation period against twenty eight licences, in respect of four licences, the export obligation achieved worked out to 38, 0.10, 83.25 and 62.77 per cent respectively.

The request for extension of export obligation period in thirty one cases was made by the licensee 3 to 26 months after the expiry of the export obligation period. The extensions ranging from twelve to forty six months were irregularly granted by the DGFT in contravention of the provisions of the Exim Policy. As exports after the expiry of the licences cannot be counted towards fulfilment of export obligation, the pro-rata customs duty amounting to Rs.41.09 crores on the material remaining unutilised upto the date of expiry of original period in respect of these 32 licences should have been recovered on the expiry of the export obligation period.

Bank Realisation Certificate as evidence of fulfilment of export obligation for US \$ 40,56,321 and Rs.147.65 lakhs were also not produced by the licensee, violating the provisions of the Exim Policy.

The irregularities were pointed out in June 1996 to the DGFT and the department. Their replies are awaited as of October 1996.

### 8.2.1 Export obligation not fulfilled

(i) As per para 63 of the Exim Policy 1992-97, export obligation is required to be fulfilled within the stipulated period of one year from the date of issue of the Advance licence. Where the export obligation is not fulfilled, both in terms of value and quantity, the licence holder is required;

- (a) to pay customs duty on the unutilised imported materials with interest at 24 per cent per annum, thereon; and
- (b) to pay to the licensing authority, an amount equivalent to the shortfall in export obligation expressed in free foreign exchange.

a) A VABAL issued to a firm on 17 May 1994, permitting import of goods upto a cif value of Rs.156.25 lakhs, prescribed an export obligation of Rs.250 lakhs, through export of 80,000 Kgs. of Sulphamethoxazole by 16 May 1995. The licensee imported duty free goods valued at Rs.54.14 lakhs but failed to effect any export even within the period extended upto 16 November 1995.

As per aforementioned provisions, the duty of Rs.53.57 lakhs along with interest thereon and an amount of Rs.86.62 lakhs, being proportionate value of shortfall in export obligation, was required to be recovered from the defaulting licensee but no action was taken for recovery of the amounts.

The matter was brought to the notice of the DGFT, and the department in July 1996. Their replies have not been received (September 1996).

b) In respect of seven VABALs issued to a tyre manufacturer between September 1992 and March 1993, imports valued at \$21,24,489 were effected. It

was noticed that imports were in excess of the limits prescribed under the licence and in addition, there was a shortfall in the export obligation amounting to \$54924 which was payable to the licensing authority in Indian currency. Customs duty on the unutilised imported materials and interest upto 31 March 1996 thereon, worked out to Rs.3.32 crores but no action was taken for recovery of the aforesaid amounts. Although the matter was reported to both the licensing authority and the customs authority in May 1996, their replies have not been received (September 1996).

### **8.2.2 Non fulfilment of export obligation**

Customs notification No.169/90, relating to the EPCG scheme stipulates that 'Capital goods' when imported into India, were eligible for concessional rate of duty at the rate of 25 per cent ad valorem and full exemption from the additional duty subject to fulfilment of certain specified conditions. Besides, in terms of the Exim Policy 1990-93, importers availing benefits of the EPCG scheme, were liable to fulfil specified export obligations within a stipulated period.

Four EPCG licence holders were allowed to import capital goods having a total cif value of Rs.12.82 crores during the years 1991 and 1992. As per the conditions prescribed in the licence, they were required to fulfil a total export obligation of Rs.55.43 crores within a period of 4 years of the imports.

It was, however, noticed that within the prescribed period, the value of exports made was only Rs.3.18 crores. The shortfall in export obligation thus worked out to Rs.52.24 crores and was pointed out to the DGFT in May 1996. The duty on the imports corresponding to the shortfall in obligations worked out to Rs.7.55 crores which was recoverable from the licencees.

Though two of the importers had executed bank guarantees for Rs.3.08 crores with the licensing authorities, these guarantees were also not enforced even for a part recovery of the duties. In other two cases, the licencees have obtained Court orders (April 1995/October 1995) restraining the competent authorities from proceeding with the recovery.

Replies of the DGFT are awaited as of September 1996.

### **8.3 Non levy of duty on imports after expiry of licence**

In terms of the Exim Policy, an import licence is valid for 12 months from the date of issue and no duty free import is to be allowed after expiry of the validity period. The said policy also provides that an advance licence which is made transferable on fulfilment of export obligation by utilising duty paid imports remains valid for the balance period or for six months from the date of 'endorsement of transferability', whichever is more.

In the course of test audit, it came to notice that in four cases in a Commissionerate, duty free imports were allowed against licences which had been endorsed for transferability in contravention of the above provisions. This resulted in irregular exemption of duty of Rs.14.33 lakhs.

The matter was pointed out to both the Licensing authority and the department in May 1996; their replies have not been received (September 1996).

#### **8.4 Availment of double benefits**

Para (v)(a) of notification No.203/92-Cus. stipulates that the export obligation is to be discharged within the period specified, by exporting goods, on which no Modvat credit has been availed in respect of inputs utilised for manufacture of the goods exported. This provision is evidently intended to ensure that no manufacturer is allowed the benefit of both duty free inputs as well as availment of Modvat credit in respect of indigenous/imported inputs. The Exim Policy 1992-97, on the other hand, envisages that an exporter, immediately after filing an application for a value based licence can claim discharge of export obligations in respect of goods already manufactured and exported by him after filing of such application. These provisions are, however, silent as to whether discharge of such obligations can be claimed prior to import of inputs.

The aforementioned provisions of the notification and the Exim Policy thus prohibit exporters only from availing double benefits of Modvat as well as duty free imports so long as the export obligations are discharged within the periods specified. Cases have come to notice where Modvat credits on inputs were availed of and the manufactured goods were exported immediately after filing of applications for issue of VABALs and thereafter the inputs were imported duty free. When the availment of such double benefits came to light, the licence holders were permitted to reverse the Modvat credits for an ex-post-facto regularisation of these transactions, although no specific provision existed for reversal of Modvat credits.

In one case, against the value based licence for duty free import of Rs.64.46 crores (cif) of inputs for manufacture of graphite electrodes, etc., the licence holder imported inputs valued at Rs.38.91 crores between November 1992 and December 1995 after he claimed discharge of export obligation to the extent of Rs.122.66 crores. It was noticed that Modvat credit of Rs.91 lakhs on indigenous input utilised for manufacture of goods exported had already been availed of. Later this credit was allowed to be reversed. In another case, a textile machinery manufacturer availed of Modvat credit of Rs.5.73 lakhs in respect of duty paid indigenous inputs for manufacture of goods exported under VABAL and thereafter

imported inputs valued at Rs.1.17 crores (cif) duty free. In this case also, the Modvat credits were allowed to be reversed so as to remove the availment of double benefits. The point to be noted in these cases is that the customs duty forgone on duty free imports (made after the exports had taken place and export obligation claimed to have been discharged) was substantially higher than the modvat credits allowed. In both cases, if the modvat credits were not allowed to be reversed for which no statutory provision exists, the duty recoverable from the licence holders would have amounted to Rs.32.72 crores.

This lacuna has been removed for imports under licences issued after 1 April 1995 under the new notifications No.79/95-Cus. and 80/95-Cus. Additional duty equal to the central excise duty leviable on the imported goods are being levied from this date and the licencees are allowed to avail of the usual benefit of the Modvat Scheme.

### **8.5 Non levy of duty on excess imports**

As per notification No.159/90-Cus., goods imported against an advance licence are exempted from the whole of the duty subject to the condition that the total cif value of goods imported does not exceed the amount specified in the licence.

A special imprest licence was issued to a unit in January 1993 for import of materials not exceeding Rs.401.30 lakhs (cif). But the unit actually imported between March 1993 and January 1994 goods valued at Rs.422.32 lakhs (cif). This exceeded the permitted limit by Rs.21.02 lakhs. The grant of duty exemption on the excess imports resulted in non levy of duty of Rs.12.06 lakhs. Interest on the amount of duty recoverable till September 1996 worked out to Rs.5.89 lakhs.

The non levy of duty and interest thereon was pointed out in audit in May 1996. Reply of the department has not been received as of September 1996.

### **8.6 Irregular imports**

Customs notification No.160/92 allows concessional rate of duty for import of capital goods which has been defined as any plant, machinery, equipment or accessory required for manufacture and includes packaging machinery, catalysts etc.

In one consignment of machinery items imported in September 1993, three items viz. Ion exchange resin, anthracite and rubber lining material did not come under the above definition of capital goods as these were raw materials and consumables. But all the items were assessed as capital goods, resulting in a short levy of Rs.1.71 crores.

On this being pointed out by audit in July 1995, the Ministry confirmed the facts and stated (January 1996) that instructions for recovering the short levied amount have been issued. Recovery particulars are awaited as of September 1996.

## **9. OTHER IRREGULARITIES**

### **9.1 Failure to re-export goods imported for exhibition/display**

As per notification No.3/89-Cus., goods intended for display or demonstration in specified events are exempt from payment of duty and additional duty subject to the condition that the importer should execute a bond for re-export of the goods within a period of six months or such extended period as may be allowed by the competent authority or pay the duty leviable in the event of failure to re-export.

In a major Custom House and its Air Cargo Complex, 57 cases of imports, allowed under the abovementioned notification involving duty of Rs.14.21 crores, were awaiting re-export between the period from January 1992 to December 1995. The normal period of six months had lapsed in respect of all these cases.

Though the department had issued demand notices amounting to Rs.544.49 lakhs in 12 cases, no cases had been adjudicated finally. In four cases, the machineries imported were allowed to be reassessed on second bill of entry. It was pointed out that no such provision for reassessment was available in the Act. The short levy of duty amounted to Rs.4.84 lakhs in these cases.

The department's reply to the audit objections issued in July 1996 has not been received (September 1996).

### **9.2 Delay in remittance of customs revenue**

A scrutiny of the challans at the office of the Pay and Accounts Officer (Customs) showed that, between May 1992 to February 1995, an amount of Rs.737.04 crores received towards customs duty by a public sector bank was not remitted immediately to the Government account. The delay ranged from 6 to 17 days and led to a loss of Rs.214.18 lakhs by way of interest at the rate of 12 per cent per annum.

The Pay and Accounts Officer, Customs stated (May 1996) that the amounts were remitted by cheques and RBI afforded credit only after realisation of such cheques.

The reply is not tenable as the duties are realised in cash or by demand draft/banker's cheques which are recognised as 'Value received instruments' by the RBI and as such there should not have been any delay in affording credit.



The PAC in their recommendation on the 'Action taken report (98th Report 10th Lok Sabha) on 'Systems defects in the working of Chief Accounting Offices' had reiterated that penal interest should be recovered in all cases of delay in remittances irrespective of the amount and period involved in the delay. An amount of Rs.214.18 lakhs was, thus, recoverable from the bank.

### **9.3 Loss of revenue on goods removed for re-warehousing**

As per section 67 of the Act read with Rule 4 of 'Warehoused Goods (Removal) Regulations 1963', goods may be removed from one bonded warehouse to another in the same or a different town, without payment of duty provided a bond is executed by the importer to the effect that he would produce to the proper officer within 3 months or within such extended period as such officer may allow, a certificate issued by the proper officer at the place of destination that the goods have arrived at that place.

In a major Custom House, 70 consignments of goods removed between March 1992 and December 1993 from one warehouse to another without payment of duty against bonds executed, the certificates of re-warehousing as prescribed were not produced within the specified period of 3 months. No extension of time for producing the re-warehousing certificates was also given. However, no action to recover the duty by invoking the terms of the bond was taken by the department. The validity of the bank guarantees furnished by the importers for the purpose of rewarehousing had also expired in all these cases. The amount of duty involved in respect of the goods removed for re-warehousing was Rs.1.90 crores.

This was pointed out by audit in January 1995. Reply of the department has not been received as of December 1996.

### **9.4 Non revision of tariff values resulting in loss of revenue**

Sub Section (2) of Section 3 of the Agricultural Produce Cess Act, 1940 authorises Government to fix values of specified items for the purpose of levy of cess from time to time. Such values should also conform to the market values in order to prevent loss of revenue. The PAC in the recommendation made in its 105th Report (7th Lok Sabha) stated that "tariff value should be kept under constant watch to make sure that they do not at any point of time lapse their relationship with the actual values."

In respect of 'Oil seed cake and meals', exported through two Custom Houses between January 1994 and January 1995, the values fixed by the Government and adopted for the purpose of levy of export cess was far below the f.o.b. values declared on the shipping bills. The f.o.b. values declared on the shipping bills were 3 to 9 times higher than the values fixed for levy of the cess.

Though notifications revising the tariff values have been issued by the Government from time to time, the value for the above mentioned goods have remained virtually the same for the past five years, as a result of which cess amounting to Rs.25 lakhs in 91 cases could not be collected.

On this being pointed out in April 1996, the department stated the obvious in May 1996 that the cess had been correctly levied as per the tariff values fixed by the competent authority under the provisions of Agricultural Produce Cess Act, 1940, for the relevant period. The department failed to address the main issue that loss of cess arose not from any violation of rules, but from lack of initiative to revise the tariff value itself.

#### **9.5 Non validation of bank guarantees resulting in loss of duty**

Three consignments of HDPE granules, imported and warehoused between February and April 1984, were allowed to be cleared provisionally after levy of only the basic duty pending decision of a High Court. The bank guarantees for Rs.7.42 lakhs given by the party as per instructions of the Court were to be revalidated till the final Court order. The High Court finally dismissed the petition of the importer on 18 October, 1991 directing payment of the differential duty along with interest at the rate of 12 per cent per annum from the date of clearance of the goods till the date of payment. The court order was received by the department only in September 1993 but the validity of the bank guarantees had expired in March/April 1992.

The department finally assessed all the bills of entries in May 1994 in terms of the Court orders and determined an amount of Rs.16.66 lakhs as the differential duty and interest.

When audit pointed out (January 1996) the failure of department to revalidate and enforce the bank guarantees in time for recovery of the short levied amount, it was stated by the department (May 1996) that action for the recovery of the amount was in progress. The department glossed over the expiry of the bank guarantees, which, if revalidated, would have eased the process of recovery.

Recovery particulars are awaited (September 1996).

#### **9.6 Non levy of duty on pilfered goods**

As per Section 45(3) of the Act, if any imported goods are pilfered after unloading in a customs bonded area while in the custody of a person referred to in sub section (1), that person shall be liable to pay the duty leviable on such goods.

Ten out of 24 drums of "Erythromycin Thiocyanate" imported in September 1995, through Bombay Air Customs were found pilfered at the time of clearance. Though a refund of Rs.9.46 lakhs, being the duty paid for the pilfered

goods, was sanctioned to the importer by the department in January 1996, no action to recover the same from the Custodian was taken.

On this being pointed out (March 1996), the department reported (May 1996) issue of a demand notice but recovery particulars are awaited (September 1996).

#### **9.7 Irregular payment of reward to government servants**

According to the Ministry's letter dated 30 March 1985, Government Servants would be eligible for rewards depending upon the contribution made by them as a team as well as individually with regard to collection of intelligence, surveillance, seizures etc. As per subsequent clarification issued by the Ministry on 14 May 1986, only outstanding contribution would qualify for grant of rewards in deserving cases in respect of post-seizure operations like investigation, adjudication and prosecution proceedings. The directive of the Board issued in February 1986 in regard to grant of such rewards also stated that "every rupee sanctioned as reward to officer/staff should deservedly be earned by them and not distributed as largesse by the authorities to their subordinates. There should be clear accountability in regard to the eligibility, quantum sanctioned vis-a-vis the inter-se role". The following illustrative cases indicates that the above directive of the Board was respected more in its breach than in its compliance.

In a major Commissionerate rewards amounting to Rs.11.82 lakhs were sanctioned (24 February 1995) to 109 officials for seizure of 3064.1 Kgs. of silver of foreign origin valued at Rs.217.55 lakhs. The seizure operation was conducted on 18 October 1991 by 16 Customs and Police officials to whom Rs.4.65 lakhs was sanctioned for their contribution to the seizure operation. Further an amount of Rs.7.16 lakhs was sanctioned to 93 other officials for their involvement in post seizure operations. While only one Preventive officer was involved in the seizure, 45 Preventive officers were involved in the post seizure operations, the nature of which had not been detailed. There was no claimant for the seized goods and the case did not involve any investigation and prosecution proceedings. The department, inspite of deployment of so many officials, adjudicated the case only in March 1994. As neither any special effort nor any contribution was made by any of the officials in the post seizure operations other than routine work, the grant of rewards amounting to Rs.7.16 lakhs for the post seizure operations was irregular and was pointed out to the department in May 1996.

The department reacted to state in July 1996 that Audit was not to sit in judgment over the decision of the reward sanctioning committee. This is clearly a misconceived idea as action of the department cannot be arbitrary, contrary to the existing directive that rewards should not be distributed on largesse.

**9.8 Non levy of penalty under section 116**

Under Section 116 of the Act, read with Section 148 *ibid* if any goods loaded in a conveyance for importation into India are not unloaded at the destination or the quantity unloaded is short and if the failure to unload or the deficiency is not accounted for to the satisfaction of Assistant Commissioner of Customs, the master of the vessel or the steamer agent is liable for penal action.

In two Commissionerates, refund claims on account of short landing were honoured without taking any penal action under section 116 against the steamer agents (December 1990 to August 1994). The department admitted the irregularities pointed out in audit during August 1995 and October 1995 and stated that penal action had been initiated against the respective carriers. The total penalty in 17 SCNs issued by one Commissionerate was Rs.12.55 lakhs. In the other Commissionerate, there was no mention of the quantum of penalty demanded in the notices issued to the carriers.

**9.9 Non disposal of uncleared goods resulting in loss of revenue**

Under section 48 of the Act, if imported goods are not cleared for home consumption or warehousing or for transshipment within 30 days of the date of import, such uncleared goods are to be disposed of after notice to the importers. An importer who filed 12 bills of entry in February 1989 for clearance of "Timber" (wood in rough) worth Rs.5.83 crores involving a duty of Rs.87.14 lakhs, cleared only a part of the goods on payment of duty of Rs.41.27 lakhs till 22 March 1991. Since the remaining goods were not cleared, the department finalised the assessment on 22 March 1991 under instructions of the Board and decided to auction them on 25 March 1991. The auction was postponed because of a court stay order against the proposed sale. Though the stay was vacated on 19 June 1991, the department did not take any further action for disposal of the goods. On 27 March 1994 a fire broke out in the port premises, as a result of which the goods were burnt.

Even after the fire, till the date of audit in November 1995, the department did not take any action either to demand the amount of duty from the importer or to approach the Insurance Company to collect the amount insured, which was claimed by the importer. Failure on the part of department to obtain a bank guarantee as instructed by the Board in August 1987 and January 1991 and to follow the provisions of section 48 strictly resulted in a loss of revenue amounting to Rs.66.62 lakhs including interest at the rate of 20 per cent per annum from 23 December 1991 (i.e. when the provisions of section 47(2) of the Act regarding payment of interest came into effect) to 27 March 1994.

The facts were brought to the notice of department in December 1995, but no final reply has been received as of November 1996.

**9.10 Excess payment of drawback of duties**

On export of goods, refund of duties of excise and customs paid on components and raw materials can be claimed as drawback as per provisions in the relevant Acts and Rules thereunder. In 8 cases of irregular or excess payment of drawback pointed out by audit, the Ministry/department accepted the audit objections involving Rs.7.13 lakhs and reported recovery of an amount of Rs.6.04 lakhs as detailed below:

(Rupees in lakhs)			
Sl. No.	Items on which Dbk was paid in excess	Amount of Dbk paid in excess	Amount of Dbk recovered
1.	Prednisolone tablets B.P. (5 mg)	0.54	0.54
2.	Ladies dresses	0.80	0.80
3.	High resolution colour graphics workstation	0.69	0.69
4.	Leather rucksacks and backpacks	0.96	0.94
5.	Leather knapsacks	0.77	0.18
6.	Leather toilet kits/bags cosmetic bags	1.00	0.52
7.	Cotton knit pyjamas	0.64	0.64
8.	Handwoven floor coverings	1.73	1.73
Total		7.13	6.04

**9.11 Miscellaneous**

450 other objections involving duty of Rs.1.64 crores were also pointed out. The department has accepted all these objections and reported recovery of an amount of Rs.1.25 crores in 425 cases.

*Vikram Chandra*

New Delhi  
The 14 February 1997

(VIKRAM CHANDRA)  
Principal Director of Receipt Audit  
(Indirect Taxes)

Countersigned

*V. K. Shunglu*

New Delhi  
The 14 February 1997

(V.K. SHUNGLU)  
Comptroller and Auditor General  
of India



## ERRATA

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55	8.2.2	18 from top	55.43	55.42
61	9.7	20 from top	11.82	11.81

01	01	20 1000000	1000	1100
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