Report of the
Comptroller and Auditor General
of India

for the year ended March 2003

Union Government

(Indirect Taxes - Customs)

No.10 of 2004

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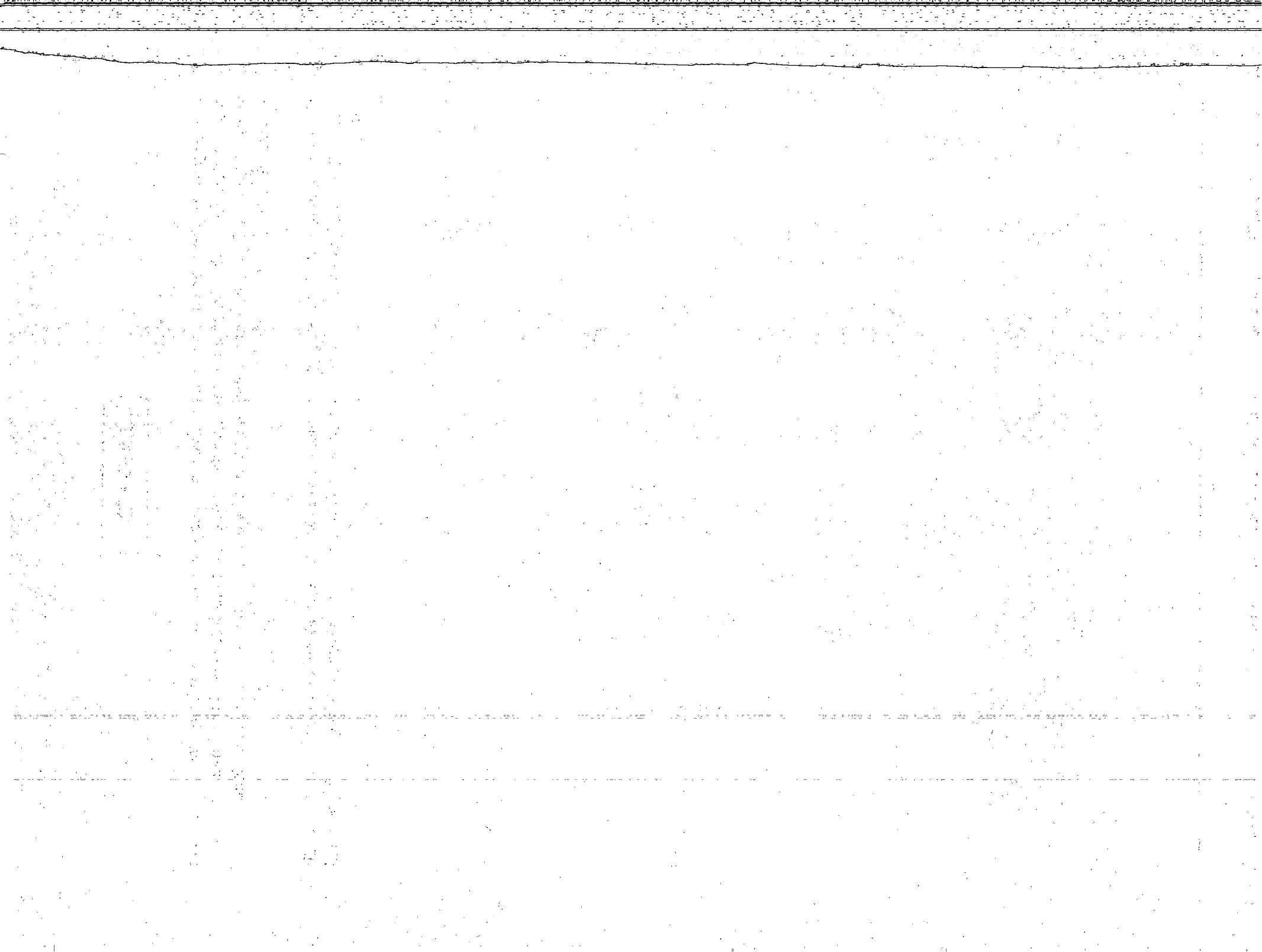
CONTENTS

PREFACE

This Report for the year ended 31 March 2003 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 2002-2003 as well as those which came to notice in earlier years but could not be reported earlier.



OVERVIEW

This report contains two reviews and 252 paragraphs involving non levy/short levy of customs duty of Rs.5862.89 crore. Some of the important audit findings included in the Report are highlighted below:

I. General

- Budget estimate 2002-03 was pitched at Rs.45,193 crore. The actual realisation fell short of budget estimates by Rs.281 crore.

{Paragraph 1.1}

- The amount of duty foregone under the various export promotion schemes during the year was Rs.27,765 crore which was 62 per cent of the total customs receipts.

{Paragraph 1.4.1}

II. Review on Software technology parks (STP) scheme

- Non utilization of imported goods by 17 units of STPI Chennai, Mumbai and Hyderabad within stipulated period under customs notification entailed recovery of duty amounting to Rs.4.74 crore besides interest of Rs.1.75 crore.

{Paragraph 2.5.1}

- Incorrect grant of exemption from payment of customs/central excise duty on ineligible goods imported/procured by 149 units entailed recovery of duty of Rs.18.08 crore besides interest of Rs.33 lakh.

{Paragraph 2.5.2 & 2.5.3}

- Due to non fulfillment of positive Export Obligation (EO) and Net Foreign Exchange Performance (NFEP) within the bonding period, 11 units of Chennai and Hyderabad STPI were liable to duty amounting to Rs.134.69 crore besides interest of Rs.138.63 crore.

{Paragraph 2.6.1}

- Non fulfillment of EO and minimum NFEP by 34 units/non submission of Softex forms by one unit entailed recovery of customs duty to the tune of Rs.63.50 crore besides interest of Rs.42.03 crore.

{Paragraph 2.6.2 & 2.6.3}

- Non levy of duty on irregular domestic tariff area (DTA) sales entailed recovery of duty amounting to Rs.1.38 crore besides interest of Rs.87 lakh from five units.

{Paragraph 2.7.1 & 2.7.2}

- Non execution of bond by three units of STPI Noida and importation of capital goods before execution of bond with customs by four units of STPI Kolkata rendered incorrect, grant of exemption of Rs.2.93 crore besides interest of Rs.1.77 crore.

{Paragraph 2.9.1 & 2.9.3}

- STPI Chennai failed to de-bond three units despite their being non operational for more than five years. The units were liable to pay customs duty amounting to Rs.2.77 crore and interest of Rs.2.11 crore.

{Paragraph 2.10.1}

- Lack of monitoring by STPI Chennai as envisaged in the guidelines resulted in non issue of show cause notices (SCN) to nine defaulter units involving duty foregone to the tune of Rs.4.56 crore.

{Paragraph 2.11.1}

- STPI Directorates failed to realise Rs.2.77 crore service charges payable by 392 units in six STPs.

{Paragraph 2.12}

III. Review on Working of inland customs bonded (public/private) warehouses

- Non observance of the provisions of the Customs Act, 1962 and instructions issued by the Ministry resulted in excess holding of goods in warehouses, improper control, non submission of bonds, non receipt of re-warehousing certificates and customs share involving revenue of Rs.4477.06 crore.

{Paragraph 3.4, 3.6, 3.7, 3.10 & 3.19}

- Goods worth Rs.206.88 crore involving duty of Rs.185.34 crore were not sufficiently safeguarded through insurance policies.

{Paragraph 3.5.1}

- Loss of revenue of Rs.50.38 crore occurred due to theft, shortage, irregular extensions/relinquishment of title to goods after warehousing and postponement of clearance of warehoused goods for availing exemptions.

{Paragraph.3.5.2, 3.8.1, 3.8.2 & 3.8.3}

- Non/short recovery of revenue amounted to Rs.9.48 crore on account of duty and interest on irregular clearance/removal of warehoused goods.

{Paragraph 3.11 & 3.12}

- Non/delayed disposal of uncleared goods and non restriction of warehousing period for perishable goods led to blockage of revenue of Rs.536.82 crore and loss of

revenue of Rs.16.27 crore. Age analysis of 2860 cases involving blockage of revenue of Rs.387.14 crore revealed that 65 per cent of revenue was blocked for more than 5 years and 29 per cent for over 10 years.

{Paragraph.3.8.4, 3.13 to 3.17}

- Non recovery of duty on shortages of liquid cargo clearance involved revenue of Rs.13.25 crore.

{Paragraph.3.9}

IV. Irregularities in assessments

- Dutiable imported goods were incorrectly classified and assessed to duty at lesser rates leading to short levy of Rs.8.51 crore in 16 cases.

{Paragraph 4.1 to 4.4}

- Extending the benefit of exemption notifications to dutiable goods not covered by them resulted in short collection of duty of Rs.3.65 crore in 33 cases.

{Paragraph 5.1 to 5.4}

- Short levy on account of undervaluation of assessable goods in 4 cases amounted to Rs.2.22 crore.

{Paragraph 6.1 & 6.2}

- Additional duty leviable under Section 3 of the Tariff Act amounting to Rs.7.94 crore was not levied/short levied in 12 cases.

{Paragraph 7.1 to 7.4}

- Special additional duty leviable under section 3A of Tariff Act amounting to Rs.18.17 crore was not levied/short levied in 6 cases.

{Paragraph 8.1 to 8.3}

V. Recoveries from defaulting export houses

- Non levy/loss of customs revenue of Rs.147.71 crore due to failure to recover benefits of export incentives under schemes like Advance Licensing Schemes and EOU from defaulting exporters.

{Paragraph 9.1 to 9.5}

VI. Other irregularities

- Irregular removal of warehoused goods, non realisation of customs share and delay in recovery of confirmed demand etc. led to loss of Rs.32.59 crore in 54 cases.

{Paragraph 10.1 to 10.14}

CHAPTER I: ANALYSIS OF RECEIPTS

1.1 Budget estimates, revised budget estimates and actual receipts

The budget estimates, revised budget estimates and actual receipts of customs duties during the year 1998-99 to 2002-03 are exhibited in the table below:-

(Rupees in crore)

Year	Budget estimates	Revised budget estimates	Actual receipts	Difference between actual receipts and budget estimates
1998-1999	48148	42648	41278	(-)6870
1999-2000	50369	47800	48334	(-)2035
2000-2001	53576	49781	47615	(-)5957
2001-2002	54822	43170	40096	(-)14726
2002-2003	45193	45500	44912	(-)281

The actual receipt of customs duties fell short of the estimates of 2002-03 by Rs.281 crore.

1.2 Trend of Receipts

A comparison of total year-wise imports with the corresponding net customs duties collected during 1998-99 to 2002-2003 has been shown in the table below :

VALUE OF IMPORTS AND IMPORT DUTY COLLECTED 1998-99 TO 2002-2003 (YEAR-WISE)

(Rupees in crore)

Year	Value of Imports	Import duties	Import duty as percentage of value of imports
1998-1999	176099	42110	23.91
1999-2000	204583	49517	24.20
2000-2001	228307	46569	20.40
2001-2002	243645	39406	16.17
2002-2003	296597	44137	14.88

1.3 Commodity wise details of customs receipts

Major commodity wise value of imports and exports and the gross duty realised therefrom during the financial year 2002-2003 and the previous year 2001-2002 are given overleaf:

1.3.1 Imports

(Rupees in crore)

Sl. No.	Commodities	Value of imports*		Import duties**		Percentage share in total import duties collection	
		2001-02	2002-03	2001-02	2002-03	2001-02	2002-03
1.	Food and live animals chiefly for food	11526.14	14003.49	4580	4236	11.62	9.60
2.	Mineral, fuels and related materials	11638.89	11605.33	2598	3191	6.59	7.23
3.	Petroleum, crude and products	66769.86	85367.00	4818	6819	12.22	15.45
4.	Chemicals and related product	16460.13	17815.98	3619	3928	9.19	8.90
5.	Manufactured goods	20445.67	29224.51	3456	3805	8.78	8.62
6.	Machinery and transport equipment	20809.14	29562.23	10400	12392	26.39	28.07
7.	Professional instruments etc.	4947.63	5167.78	2650	2907	6.72	6.59
8.	Others	91047.38	103850.62	7285	6859	18.49	15.54
	Total	243644.84	296596.94	39406	44137		

1.3.2 Exports

(Rupees in crore)

Sl. No.	Commodities	Value of exports*		Export duty and cess**	
		2001-02	2002-03	2001-02	2002-03
1.	Food items	20458.41	24108.63	08	07
2.	Beverages and tobacco	1439.33	1163.05	08	07
3.	Petroleum, crude and products (including mica)	55.22	39.84	02	02
4.	Others	185792.60	227478.45	117	138
	Total of exports and re-exports	207745.56	252789.97	135	154

Source - *Ministry of Finance, New Delhi.
**Directorate of Data Management, Central Excise and Customs, New Delhi.

1.4 Duty foregone

1.4.1 Under export promotion schemes

(a) The break-up of the duty foregone for export promotion schemes viz., advance licence, duty exemption pass book (DEPB), export promotion capital goods (EPCG), export promotion zone (EPZ), export oriented units (EOUs) and refund of duty under the drawback and other schemes for the period from 1999-2000 to 2002-2003 are shown in the table overleaf:

CUSTOMS DUTY FOREGONE UNDER EXPORT PROMOTION SCHEMES AND DUTY DRAWBACK SCHEME

(Rupees in crore)

Year	Advance licence & others	DEPB	EPCG	EPZ	EOU	Duty Drawback	Total
1999-2000	4513	4063	1299	1096	2938	4257	18166
2000-2001	5612	4631	1513	1223	3537	4189	20705
2001-2002	7890	5661	2008	2064	4219	2957	24799
2002-2003	7462	6831	3026	1106	4820	4520	27765

(b) The total duty foregone under various export promotion schemes for the period 1999-2000 to 2002-2003 as a percentage of customs receipts is shown in the table below:

CUSTOMS DUTY FOREGONE

(Rupees in crore)

Year	Customs duty collected	Total duty foregone under export promotion schemes	Duty foregone as a percentage of customs receipts
1999-2000	48334	18166	38
2000-2001	47615	20705	43
2001-2002	40096	24799	62
2002-2003	44912	27765	62

Duty foregone under export promotion schemes has gone up from 38 per cent of customs duty receipts in 1999-2000 to 62 per cent of customs receipts in 2002-2003.

1.4.2 Other duty foregone

Duty foregone under Section 25 (1) and (2) of the Customs Act, 1962 {other than for export promotion schemes vide para 1.4.1 (b)} during 1999-2000 to 2002-2003 are shown in the table below:

(Rupees in crore)

Year	No. of notifications issued under 25(1)	No. of total notifications issued under 25(2)	Total No. of notifications issued	Duty foregone under 25(1)	Duty foregone under 25(2)	Total Duty foregone
1999-2000	66	NA	NA	4156	NA	NA
2000-2001	60	NA	NA	6733	NA	NA
2001-2002	39	NA	NA	2477	NA	NA
2002-2003	54	NA	NA	3512	NA	NA

Section 25(1) General exemption
Section 25(2) Adhoc exemption

1.5 Cost of collection of customs receipts

The expenditure incurred on collection of customs duty during the year 2002-2003 alongwith the figures for the previous year are given below:

(Rupees in crore)

Cost of collection	2001-2002	2002-2003
Revenue cum import export and trade control functions	123.23	131.61
Preventive and other functions	239.62	270.33
Total	362.85	401.94
Cost of collection as percentage of Customs receipts	0.90	0.89

1.6 Searches and seizures

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

SEARCHES AND SEIZURES

Sl. No.	Description	2001-2002	2002-2003
1.	Number of searches	2143	1379
2.	Value of goods seized (Rupees in crore)	737.00	448.00
3.	Number of seizure cases adjudicated	7695	4797

These figures relate to 61 Custom houses/Commissionerates

1.7 Arrears of customs duty for recovery

The amount of customs duty assessed upto 31 March 2003 which was still to be realised as on 30 June 2003 was Rs.1265.19 crore in 30 Custom houses.

1.8 Demands of duty barred by limitation

Demands raised by the Department up to 31 March 2003 which were pending realisation as on 30 June 2003 and where recovery was barred by limitation amounted to Rs.2 lakh in 19 Custom houses and Commissionerates.

1.9 Duty written off

Customs duties written off, penalties waived and exgratia payments made during the year 2002-2003 and the preceding two years are given below:

(Rupees in lakh)

Year	Amount
2002-2003	36.08
2001-2002	14.38
2000-2001	60.67

1.10 Number of pending audit objections

The number of audit objections raised upto 31 March 2003 and pending settlement as on 30 September 2003 in the various Custom houses and combined commissionerates of Central Excise and Customs are given below:

OUTSTANDING OBJECTIONS AND AMOUNT INVOLVED

(Rupees in crore)

Sl. No.	Commissionerate	Number	Amount
1.	Ahmedabad (Prev.)	28	14.04
2.	Ahmedabad	38	31.97
3.	Cochin	98	56.31
4.	West Bengal (Prev.)	369	66.19
5.	Bangalore	390	141.51
6.	Mumbai(Air)	449	10.73
7.	Hyderabad	566	580.01
8.	Mumbai(Sea)	704	280.67
9.	Kolkata	1320	906.21
10.	Chennai (Sea)	1513	216.47
11.	Delhi	1556	69.18
12.	Others	2110	1588.89
	Total	**9141**	**3962.18**

1.11 Categories of outstanding audit objections

(Rupees in crore)

Sl. No.	Categories of objections	No. of objections	Amount
1.	Short levy due to misclassification	1802	66.42
2.	Short levy due to incorrect grant of exemption	985	243.60
3.	Non levy of import duties	1288	113.52
4.	Short levy due to undervaluation	365	28.12
5.	Irregularities in grant of drawback	997	16.18
6.	Irregularities in grant of refunds	50	19.65
7.	Irregularities in levy and collection of export duty	13	6.42
8.	Other irregularities	3641	3468.27
	Total	**9141**	**3962.18**

1.12 Contents of the report

The Report includes two reviews, 'Software technology parks (STP) scheme' and 'Working of inland customs bonded (public/private) warehouses', highlighting leakage of revenue to the tune of Rs.5639.56 crore. Besides there are 252 paragraphs (including 71 cases of Total Under Assessment) featured individually or grouped together, arising from important findings from test check in audit pointing out leakage of revenue aggregating Rs.222.42 crore. Of this the Department/Ministry of Finance had till February 2004 accepted audit observations in 165 paragraphs involving non/short levy of duty of Rs.132.23 crore and reported recovery of Rs.8.70 crore.

CHAPTER II: SOFTWARE TECHNOLOGY PARKS (STP) SCHEME

2.1 Highlights

- **Non utilisation of imported goods by 17 STP units of Chennai, Mumbai and Hyderabad within stipulated period under customs notification entailed recovery of duty amounting to Rs.4.74 crore besides interest of Rs.1.75 crore.**

(Paragraph 2.5.1)

- **Incorrect grant of exemption from payment of customs/central excise duty on ineligible goods imported/procured by 149 units entailed recovery of duty of Rs.18.08 crore besides interest of Rs.33 lakh.**

(Paragraph 2.5.2 & 2.5.3)

- **Availment of exemption from central excise duty without prior permission of STPI and irregular exemption from duty on imported goods used exclusively for commercial training without achievement of minimum net foreign exchange earning as a percentage of exports (NFEP) entailed recovery of duty amounting to Rs.90.25 lakh apart from interest of Rs.20.89 lakh.**

(Paragraph 2.5.4 & 2.5.5)

- **Due to non fulfilment of positive export obligation (EO) and NFEP within the bonding period, 11 units of Chennai and Hyderabad STPI were liable to pay duty amounting to Rs.134.69 crore besides interest of Rs.138.63 crore.**

(Paragraph 2.6.1)

- **Non fulfilment of minimum EO and NFEP by 34 units/non submission of Softex forms by one unit entailed recovery of customs duty to the tune of Rs.63.50 crore besides interest of Rs.42.03 crore.**

(Paragraph 2.6.2 & 2.6.3)

- **Non levy of duty on irregular domestic tariff area (DTA) sales entailed recovery of duty amounting to Rs.1.38 crore besides interest of Rs.87 lakh from five units.**

(Paragraph 2.7.1 & 2.7.2)

- **Non execution of bond by three units of STPI Noida and importation of capital goods before execution of bond with customs by four units of STPI Kolkata rendered incorrect grant of exemption of Rs.2.93 crore besides interest of Rs.1.77 crore.**

(Paragraph 2.9.1 & 2.9.3)

- **STPI Chennai failed to de-bond three units despite their being non operational for more than five years. The units were liable to pay customs duty amounting to Rs.2.77 crore and interest of Rs.2.11 crore.**

(Paragraph 2.10.1)

- **Lack of monitoring by STPI Chennai as envisaged in the guidelines resulted in non issue of SCNs to nine defaulter units involving duty foregone to the tune of Rs.4.56 crore.**

(Paragraph 2.11.1)

- **STPI Directorates failed to realise Rs.2.77 crore service charges payable by 392 units in six STPIs.**

(Paragraph 2.12)

2.2 Introduction

The STP Scheme was launched with the primary objective of boosting software/hardware export including export of professional services using data communication links or physical forms. The scheme is administered by the Department of Electronics, through Directors of respective Software Technology Parks which form part of the Software Technology Parks of India, a society established by the Department of Electronics, Government of India and registered under the Society Registration Act, 1860. The scheme integrates the concepts of hundred per cent EOUs and EPZs of the Government of India and the concept of Science Parks/Technology Parks as operating elsewhere in the world. The monitoring of progress of software exports is the responsibility of the Director of STPI. Department of Electronics is to furnish every month detailed information on all the applications for software exports and the progress of action thereon is reported to the Cabinet Secretariat and to the Ministry of Commerce for being placed before the Empowered Committee of Secretaries on exports. The Director of STPI has to forward the case of defaulting unit to DGFT to take penal action for non fulfilment of conditions of Letter of Approval (LOA).

2.3 Audit Objectives

A comprehensive review on the working of STP Scheme was conducted to seek assurance that:

(i) the units fulfilled the import conditions as laid down in the relevant notifications,

(ii) the scheme as a whole in its planning and implementation achieved the objective of promoting export of software and hardware and

(iii) The systems of internal controls and monitoring were effective.

2.4 Audit Coverage

Of 7385 units registered in 11 STPI Directorates, 4400 units were operational, of which 1290 units {(1251 STP, 39 Electronic Hardware Technology Park (EHTP)} were covered in audit. Records of these Directorates were also test checked during August 2002 to June 2003.

Audit findings are contained in the succeeding paragraphs.

2.5 Importability of Goods

2.5.1 Non utilisation of imported goods within the stipulated period

According to condition 7 under paragraph 1 of notification No.140/91-Cus dated 22 October1991, if imported capital goods are not installed or otherwise utilised within the bonded premises or not re-exported within a period of one year from the date of importation, or within such extended period as may be allowed by the Assistant Commissioner of Customs, an amount equal to customs duty leviable on unutilised goods and interest at 20 per cent per annum on such duty shall be demanded from the importer.

It was noticed that 17 units (Chennai 14, Mumbai 1, Hyderabad 2) had not utilised imported capital goods worth Rs.10.57 crore within the stipulated period of one year. So, duty amounting to Rs.4.74 crore besides interest of Rs.1.75 crore were recoverable from the units.

A few cases are narrated below:

(a) M/s. Ambal Transcripts Private Limited, (STPI Chennai), had imported capital goods worth Rs.13.36 lakh during 2000-2001 but failed to utilise them as of March 2003. Therefore, customs duty amounting to Rs.7.35 lakh besides interest of Rs.3.31 lakh was recoverable from the unit.

(b) Similarly, M/s. ELGI Software and Technologies Limited, (STPI Chennai), had imported capital goods worth Rs.39.26 lakh during 2000-2001, which remained unutilised as of March 2003. Customs duty amounting to Rs.21.59 lakh besides interest of Rs.9.72 lakh was recoverable from the unit.

On this being pointed out in June 2003, the Department reported that the performance of the unit would be analysed and action initiated.

(c) Two STP units, M/s. Sneha ERP Technology and M/s. ATMT Software Limited, (STPI Hyderabad) imported capital goods valued at Rs.39.03 lakh between September 1997 and December 1999 but failed to utilise the same as of May 2003. Hence, duty amounting to Rs.18.83 lakh was recoverable besides interest due thereon.

On this being pointed out in June 2003, customs department stated in one case that recovery action was being taken and in the other case imported goods were transferred to another unit with permission of Director STPI whose reply was awaited (February 2004).

(d) M/s. BHA Group Intel. Private Limited, (STPI Pune) had imported capital goods worth Rs.5.23 lakh during 1998-99 but failed to utilise them as of March 2003. So, duty amounting to Rs.2.45 lakh was recoverable besides interest due thereon.

On this being pointed out in June 2003, the Department stated that the demand notice was issued to the party.

2.5.2 Incorrect grant of exemption from payment of customs duty to ineligible items

Notification dated 22 October 1991 exempts certain categories of goods from import duty when imported by an STP unit for development and export of software. The above notification was amended on 22 May 2000 to include some additional items viz. accessories of capital goods such as PABX, video projection system, uninterrupted power supply system (UPS), tele conference equipments and security system. There was further amendment of the notification in October 2001 to include certain more items like networking equipment, data transfer protocol equipments and central air conditioning equipments.

Test check of records however revealed that 77 units (Kolkata/Bhubaneswar 16, Bangalore 3, Hyderabad 33, Pune 7, Mohali 1, Trivandrum 17) had availed customs duty exemption on capital goods worth Rs.22.03 crore even when they were not covered under the relevant extant notifications. Therefore, duty amounting to Rs.13.11 crore was recoverable besides interest of Rs.33 lakh.

Some illustrative cases are as follows:

(a) A unit, M/s. CA-TCG Software, Limited, (STPI Kolkata) imported sound card, SDRAM plug etc., (computer accessories) during 1999-2000 for a value of Rs.42.03 lakh, when exemption was not eligible. Hence, duty foregone amounting to Rs.19.83 lakh was recoverable.

(b) Another unit, M/s. Infosys Technologies Limited, (STPI Bhubaneswar) had imported EPABX, UPS system, video conferencing equipments, in-focus, power view and computer accessories for a total value of Rs.52.83 lakh during May 1997 to January 2000. The above items were not eligible for exemption till the issue of notification of 22 May 2000. So, duty amounting to Rs.32.04 lakh was recoverable.

(c) M/s. Quark Media House (India) Limited, (STPI Mohali) had imported networking equipment system during 1998-99 for a total value of Rs.26.66 lakh which became eligible for exemption only in October 2001. Therefore, the duty foregone amounting to Rs.17.92 lakh was recoverable.

(d) M/s. Cognizant Technology Solutions, (STPI Kolkata) had imported networking equipment, control adopter, structure cable, fibre components, data cum parts and accessories, printed circuit assemblies etc., during October 1996 to August 1999 for a total value of Rs.96.94 lakh. The goods were included vide notifications dated 22 May 2000 and 10 October 2001. So, availing of duty exemption prior to May 2000 was not in order and duty amounting to Rs.42 lakh was recoverable.

On this being pointed out in audit (February 2003) the Commissionerates of Customs Bhubaneswar and Hyderabad and STPI Directorates replied that the said goods were included in the broad list of capital goods. The replies are not tenable because the Exim policy issued by the Ministry of Commerce and Industry contains general guidelines whereas the eligibility of a particular good for duty free import or otherwise should be read with the relevant customs notifications.

In other cases replies were awaited (February 2004).

2.5.3 Incorrect grant of exemption from payment of central excise duty

Annexure 1 of Central Excise notification dated 4 January 1995 includes capital goods, material handling equipments, captive power plant, office equipments, raw materials etc and some specified goods as exempted from payment of central excise duty. The above notification was further amended on 22 May 2000 to include certain additional items like UPS, EPABX, panels for electricals and air conditioners.

Test check revealed that 72 units (Kolkata 3, Bhubaneshwar 3, Hyderabad 52, Mumbai and Pune 14) had availed duty exemption on procurement of indigenous goods worth Rs.22.61 crore prior to the amendment of the then extant notification. As a result, a sum of Rs.4.97 crore being the amount of incorrect exemption of central excise duty was recoverable apart from interest due.

Some illustrative cases are narrated below:

(a) Two companies, M/s. Cognizant Technology Solutions and M/s. Tata Consultancy Service Limited, (STPI Kolkata), had procured lift components and water treatment plant worth Rs.27.09 lakh during August and November 2002 without payment of central excise duty which were not covered under the extant notification and central excise duty amounting to Rs.4.33 lakh was recoverable.

On this being pointed out (May 2003), STPI, Kolkata admitted (June 2003) that the impugned goods were not specifically mentioned in the relevant list of exemption notification and that they were allowed exemption benefit on the analogy of DG sets and air-conditioners. The reply is not tenable since there can be no exemption on items which are not covered under the rules on grounds of such analogies.

(b) M/s. Satyam Computer Services Limited, (STPI Pune) procured UPS systems, batteries etc., for a value of Rs.29.26 lakh prior to 22 May 2000, the date of the exemption notification. Hence, duty amounting to Rs.5.15 lakh was recoverable.

On this being pointed out (June 2003), the Department stated that UPS was treated as a capital good. The reply is not tenable, as UPS was not included in the list of capital goods till amendment was effected through notification of 22 May 2000.

2.5.4 Inadmissible exemption from central excise duty

According to procedure laid down in condition No.2 of Central Excise notification dated 04 January 1995, the unit was required to obtain permission from the STPI for purchase of goods required for the development and export of software from the DTA against CT 3 form in order to avail exemption from payment of central excise duty.

It was noticed that two units, M/s. Infosys Technologies Limited and M/s. Quark Media House Private Limited, (STPI Mohali), had procured indigenous goods for a total value of Rs.3.12 crore against CT 3 form obtained directly from the central excise department and availed central excise duty exemption without obtaining prior permission from STPI, which was in violation of the provisions. Duty amounting to Rs.52.96 lakh and interest of Rs.20.89 lakh were recoverable. It was noticed that ex post facto sanction had not been sought and no reply from Director STPI was forthcoming.

2.5.5 Irregular exemption from duty on imported goods used exclusively for commercial training

Customs notification dated 22 October 1991, stipulated that imported goods were to be used for development of software and other specified activities for export out of India. However, according to condition No.14 inserted through notification No.12/98-Cus dated 27 April 1998, the Assistant/Deputy commissioner of customs could permit use of computer systems for training purpose (including commercial training) subject to achievement of minimum NFEP[1] and the goods having been utilised within the bonded premises.

M/s. Keane India Limited, (STPI Hyderabad) had imported capital goods valued at Rs.86.13 lakh and utilised the same for commercial training in a training center namely "Keane School of Excellence" for which a separate customs bonded warehouse licence was obtained. Since the said training center did not perform any specified activity for export nor did it obtain permission of customs to use the capital goods for training purpose, the duty exemption availed by it to the tune of Rs.37.29 lakh was not in order and hence recoverable from the unit, apart from the interest and penalty due.

This was pointed out in January 2003, reply of the Department was awaited (February 2004).

2.6 Non fulfilment of EO and NFEP

According to para 98/9.6 of Exim Policy (1992-97 and 1997-2002) read with para 178/9.20 of the Hand Book of Procedure (HBP) Volume I, an STP unit is required to execute a legal undertaking (LUT) with Director STPI and a bond with Customs under relevant customs notifications. According to paras 4 and 7 of LUT, the STP/EHTP units, in the event of failure to fulfil the EO/NFEP and conditions stipulated in the notification and those under the said Exim Policy as amended from time to time and conditions for establishment of technology parks for software exports as specified by the Department of Electronics, have to pay to the Government, customs duty leviable at the relevant time of import along with interest,

[1] Net foreign exchange earning as a percentage of exports

liquidated damages as determined by the Director STPI and penalty as decided by the Director General of Foreign Trade (DGFT)/Inter Ministerial Standing Committee (IMSC) New Delhi under Section 11(2) of the Foreign Trade (Development and Regulations) Act 1992.

Several instances of non fulfilment of aforesaid provisions were noticed:

2.6.1 Non fulfilment of positive EO and NFEP

In accordance with condition No.7 (iv) under customs notification dated 22 October 1991 read with notification dated 22 March 1994 issued by the Ministry of Commerce, the STP units in the event of failure to fulfil the EO equal to 1.5 times of the value of hardware imported plus 1.5 times of wage bill and prescribed net foreign exchange earning as a percentage of exports within the bonding period of five years, have to pay to Government, duty relevant at the time of import and interest at 20 per cent besides penalty.

Test check revealed that, 11 units (Chennai 10, Hyderabad 1) had not achieved positive EO/NFEP and were in fact negative foreign exchange earners and were liable to pay customs duty of Rs.134.69 crore and interest amounting to Rs.138.63 crore. Besides, penalty was also leviable.

A few illustrative cases are narrated below:

(a) An STP unit, M/s. SRM Systems and Software Limited, (STPI Chennai) which was issued letter of permission (LOP) on 23 March 1998, imported duty free capital goods to the tune of Rs.59 lakh and incurred an expenditure of Rs.90.30 lakh towards the wage bill. The foreign exchange outflow of the unit was Rs.4.57 crore. It could achieve exports to the tune of Rs.1.22 crore only against the specified EO of Rs.2.24 crore, thus, rendering duty amounting to Rs.24 lakh and interest to the tune of Rs.13 lakh recoverable.

On this being pointed out (November 2002), the STPI Directorate replied that, the case was referred to DGFT for penal action. However, customs duty and interest were not recovered yet (February 2004).

(b) An EHTP unit, M/s. ELCOT Power Controls Limited, Salem, was issued LOP on 16 September 1994 by STPI Chennai, and they imported capital goods worth Rs.10.45 crore. The actual exports made by the unit were to the tune of Rs.5.98 crore. The unit had achieved value addition of (-) 74.98 per cent against the minimum value addition required of 15 per cent. So, duty amounting to Rs.3.50 crore and interest of Rs.5.07 crore were recoverable.

On this being pointed out (November 2002), the Directorate replied that the Assistant Commissioner of central excise Salem division had started action by serving show cause notice but the unit had not responded. Customs duty and interest were yet to be recovered, besides penalty being due (February 2004).

(c) M/s. Pramati Technologies Private Limited, an STP unit, was issued LOP on 27 April 1997 by Director STPI, Hyderabad and they imported capital goods worth Rs.1.39 crore.

Against an EO of Rs.14.65 crore their achievement was only Rs.1.93 crore and the net foreign exchange earned by the unit was (-) Rs.2.29 crore due to huge amount of foreign exchange outflow amounting to Rs.4.22 crore on goods other than capital goods. As the unit had failed to achieve positive net foreign exchange during the operation of five years, the duty amounting to Rs.34 lakh on imported goods was to be recovered besides interest due and penalty thereon.

On this being pointed out (May 2003), STPI, Hyderabad stated (August 2003), that the case for renewal for further five years without fulfilling EO was forwarded to Inter Ministerial Standing Committee (IMSC) for approval and final decision was awaited.

2.6.2 Non fulfilment of EO and minimum NFEP

Test check revealed that 34 Units (Chennai 12, Kolkata 6, Bhubaneswar 1, Bangalore 3, Hyderabad 4, Gandhinagar 4, Pune 1, Trivandrum 2, Noida 1) which had completed five years of commercial production prior to March 2003 had not fulfilled their EO/NFEP. So, customs duty amounting to Rs.63.31 crore and interest of Rs.41.81 crore was recoverable from the units, besides penalty.

Instances noticed by audit included the following:

(a) An STP unit M/s. Saturn Information India Limited, who was issued LOP on 18 December 1995 by STPI Director Chennai, had imported capital goods for a total value of Rs.2.03 crore. The unit exported goods worth Rs.2 crore upto November 2001 against requirement of Rs.3.05 crore leading to a short fall of Rs.1.05 crore. Therefore, the duty foregone of Rs.68 lakh and interest of Rs.68 lakh were recoverable.

On this being pointed out (November 2002), Director STPI accepted (July 2003) that the unit had not met the stipulated EO and began penal action against the unit. Recovery particulars are awaited.

(b) M/s. Transys Information Private Limited, who was issued LOP on 31 March 1997 by STPI Chennai imported capital goods worth Rs.1.04 crore. During five years of commercial production, the unit earned foreign exchange to the tune of Rs.23.76 crore against EO of Rs.61.10 crore resulting in a shortfall of Rs.37.34 crore. Hence, customs duty of Rs.42 lakh availed by the unit and interest of Rs.38 lakh were recoverable.

This was pointed out in audit in June 2003, the reply was awaited (February 2004).

(c) M/s. Globsyn Technologies Limited, which was issued LOP in April 1997 by STPI Kolkata imported capital goods worth Rs.3.52 crore and incurred an expenditure of Rs.5.75 crore towards the wage bill. The unit could earn foreign exchange only to the extent of Rs.12.85 crore against requirement of Rs.13.90 crore resulting in shortfall to the tune of Rs.1.05. crore. Therefore, the duty foregone of Rs.1.49 crore and interest of Rs.1.77 crore were recoverable apart from penalty.

This was pointed out in June 2003, the reply was awaited (February 2004).

(d) M/s. GPS Usha Limited, who were issued LOP on 27 November 1996 by STPI Bangalore, imported capital goods worth Rs.87.32 lakh. The unit could earn net foreign exchange to the tune of Rs.2.16 crore against the EO of Rs.2.52 crore resulting in shortfall to the extent of Rs.36 lakh. Thus, duty foregone of Rs.4.86 lakh besides interest due thereon were recoverable apart from penalty.

This was pointed out in May 2003, the reply was awaited (February 2004).

2.6.3 Non ascertaining of EO due to non submission of Softex forms to STPI

Director STPI is the authority to certify the correctness of value of software exported. On export of software through data communication or telecommunication network, an export declaration viz., SOFTEX prescribed by the RBI is required to be submitted to him for attestation within 30 days from the date of invoice.

Audit noticed a case wherein a unit M/s. Haystock Software Systems Private Limited, (STPI, Chennai) was issued LOP on 20 December 1993 and had imported capital goods worth Rs.32.55 lakh during the period of five years. Though, it had reportedly exported software worth Rs.8.38 crore upto 1998-99 it had not submitted SOFTEX form to the STPI for attestation rendering the correctness of value of exports unascertainable. The unit could not be considered as having fulfilled the EO. The duty foregone amount of Rs.19.26 lakh and interest of Rs.21.64 lakh were recoverable.

This was pointed out in June 2003, reply was awaited (February 2004).

2.7 DTA Sale

According to para 102(d) of Exim Policy and para 183 of HBP Volume I (1992-97), DTA sale permission shall be subject to achievement of the value addition prescribed. Further, in terms of guidelines for sale of goods in the DTA[2] (Appendix XXXIII) of HBP Volume I (1992-97), the sale would be permissible only if the value addition achieved by the unit was not less than the minimum of 20 per cent. Under para 9.9 (d) of Exim Policy (1997-2002) NFEP to be achieved by the unit was reduced from 20 to 15 per cent. According to para 9.9 of the Exim Policy and 9.23 of HBP Volume I read with Appendix 42 ibid, STP units are permitted to sell in DTA upto the 25 per cent of the FOB value of exports subject to payment of applicable duties. The limit of DTA sale was raised to 50 per cent from 1 April 1999 onwards.

2.7.1 Non levy of customs duty on irregular DTA sale

Two EHTP units, M/s. Pentamedia Graphics Limited and M/s. Qmax Test Equipments Private Limited, (STPI Chennai) had effected DTA sale to the tune of Rs.16 crore availing duty concession to the extent of Rs.90 lakh (differential duty). Since, the units had not achieved the prescribed value addition, they were not entitled for DTA sale rendering duty concession availed of by them amounting to Rs.90 lakh and interest of Rs.84 lakh as recoverable.

[2] Domestic Tariff Area

On this being pointed out (November 2002), the STPI Directorate stated that, the DTA sale permission (for the first five years) had been accorded by CMD Electronics Corporation of Tamil Nadu who was then the designated officer for implementing EHTP Scheme in the State till July 1999 and only thereafter was the activity transferred to STP Directorate.

The reply is not tenable because Director STPI should have, in any case, obtained reasons for penal action not having been begun from erstwhile designated officer against the defaulting unit.

2.7.2 Irregular duty concession on DTA sales

Test check of records revealed that three STP units (one each in STPI Kolkata, Gandhinagar, and Trivandrum) had effected DTA sale to the extent of Rs.1.33 crore in excess of prescribed limit of 25 per cent. They were liable to pay duty amounting to Rs.47.83 lakh besides interest of Rs.3.49 lakh in one case.

A few cases are narrated below:

(a) An STP unit M/s. Interra Information Technologies (India) Private Limited, (STPI Kolkata) had effected DTA sale for a total value of Rs.51.79 lakh during 1996-97 without permission of STPI and without payment of any duty. The quantum of this sale also exceeded the permissible limit of 25 per cent. (Rs.38.04 lakh). This led to non levy of duty of Rs.6.21 lakh.

This was pointed out (April 2003), the reply was awaited (February 2004).

(b) An STP unit, M/s. Enter Technologies Private Limited, (STPI Trivandrum), had effected DTA sale for a total value of Rs.53.63 lakh against the eligible limit of Rs.6.90 lakh, which was 677 per cent above the said limit, without obtaining permission of the STPI and without fulfilling the EO. This was in violation of bond conditions and the unit was liable for penal action. The duty foregone on capital goods amounted to Rs.32.67 lakh besides interest due thereon.

2.7.3 DTA sales in excess of permissible limit

Five units under the jurisdiction of STPI Kolkata had exceeded DTA sale limit to the tune of Rs.14.89 crore. Such irregular DTA sale was indicative of lack of proper control by the STPI Directorate.

This was pointed out in May 2003, the reply was awaited (February 2004).

2.7.4 DTA sale without permission of Director STPI

Test check of records revealed that 39 units (Chennai 2, Kolkata 5, Bhubaneswar 2, Bangalore 2, Hyderabad 14, Noida 5, Mumbai 9) had made DTA sales to the tune of Rs.87.55 crore without obtaining permission of Director STPI.

In the case of a unit under STPI Pune, Central Excise Department stated that software cleared in DTA was duty free and within permissible limit under Exim policy. Even so, action for effecting DTA sale without permission should have been started under the provisions of Exim policy.

Director STPI, Hyderabad admitted (August 2003) the irregular DTA sale and stated that action would be taken by IMSC[3]. In other cases reply was awaited (February 2004).

2.8 Loss of Government revenue

2.8.1 Due to sale of imported material after allowing depreciation

Provisions of Exim policy stipulate that capital goods and spares that have become obsolete/surplus, may either be exported or disposed of in DTA on payment of applicable duties. The benefit of depreciation, as applicable, is available in case of disposal in DTA only.

M/s. Tyco Electronics Limited, an EHTP unit (STPI Bangalore) imported capital goods during June 1998 to April 1999 with some of the said goods being sold (July 1999) to M/s. AMP Japan and M/s. Tyco-USA at the import price after allowing depreciation and without having been used for the purpose envisaged in import permission on the plea that the goods had become obsolete. Sale of duty free imported goods outside India instead of in DTA and availing depreciation was not in order.

2.8.2 Due to disposal of waste/scrap in excess of the prescribed limit

An STP unit can export or sell in DTA, the scrap or waste arising out of production on payment of duty. Norms for waste of imported goods (inputs) for an export product find place in Appendix 41 of HBP Vol.I. According to item 101 of the Appendix, the prescribed limit for percentage of wastage is 5 only.

A test check of records revealed that, a unit M/s. Torroid (India) Limited, (STPI Trivandrum) had availed excess wastage ranging from 7 to 13 percent on copper weighing 583079 kilograms used in the manufacture of transformers during 1999-2002. Duty-foregone amount of Rs.39.41 lakh being duty exemption availed on the excess quantity of copper was recoverable from the unit.

This was pointed out in May 2003, reply was awaited (February 2004).

2.9 Execution of bond/bank guarantee (BG)

2.9.1 Non execution of bond

According to CBEC Circular of 10 March 1998 as amended on 17 November 1999, STP/EHTP units were required to execute a single B-17 bond for a value equivalent to 25 per

[3] Inter Ministerial Standing Committee

cent of the amount of duty leviable on permitted goods meant for re-warehousing or a security (BG or any other recognised security) to the extent of 5 per cent of value of bond.

(a) Two units M/s. Alstom Systems Limited and M/s. R. System International Limited, (STPI Noida), took over from their predecessor company on 26 April 2000 and 28 August 2000 respectively and imported goods valued at Rs.21.52 lakh and Rs.1.42 crore respectively without execution of requisite bond and BG. Duty involved in these two cases works out to Rs.63.99 lakh.

(b) A unit, M/s. HCL Perot Systems Private Limited, (STPI Noida) had imported capital goods worth Rs.2.34 crore involving duty of Rs.75.60 lakh during the period May 1998 to August 1999 without executing a valid bond.

This was pointed out in May 2003; the reply was awaited (February 2004).

2.9.2 Delayed execution/delayed renewal/non-renewal of bond

Four units under STP, Kolkata had delayed execution of bond with the customs authority for a period ranging from 14 to 43 months after executing LUT with STP, Kolkata. Of these, one had delayed renewal by 3 months and another unit did not renew its bond upto February 2003 after the expiry of its initial bonding period on 31 December 2001. Two other units did not renew their bond upto January 2003 and February 2003 after their expiry on 4 October 2001 and 31 January 2002, respectively.

This was pointed out in June 2003, the reply was awaited (February 2004).

2.9.3 Importation before execution of bond

According to condition No.2 read with condition No.7 stipulated in customs notifications both dated 22 October 1991, the goods specified therein when imported into India by an STP unit for the purpose of carrying out certain specified activities would be exempted from the whole of the customs duty and additional duty leviable thereon provided the importer executed a bond with customs, binding himself, to pay on demand an amount equal to the duty leviable on the said goods and interest thereon at the prevalent rate.

Four STP units under the jurisdiction of STPI Kolkata had imported capital goods worth Rs.3.78 crore between September 1997 and May 2000 before execution of bond with the customs department violating the conditions of the notifications. Lack of proper safeguard while granting exemption without verification of bond by customs authorities led to availing of incorrect duty exemption by the units from whom duty amounting to Rs.1.53 crore and interest of Rs.1.77 crore was recoverable.

This was pointed out in June 2003, reply was awaited (February 2004).

2.9.4 Unauthorised operation of STP units without customs bonding

Para 9.18 of HBP Vol. (I) 1997-2002 stipulates that the entire operation of STP/EHTP unit should be in a customs bonded premises unless otherwise specially exempted.

Nineteen units under the jurisdiction of STPI Hyderabad, had incorrectly carried out their business without obtaining a customs bonded warehouse licence for their premises. Therefore, the export for a value of Rs.161.54 crore made by these units during 1997-98 to 2001-2002 did not qualify for EO. Issue of export clearance certificates by Director, STPI for consideration of such exports for EO was not in order.

On this being pointed out in June 2003, Director STPI Hyderabad while admitting the audit point stated that Department of Information Technology, New Delhi had been approached for ratification.

2.9.5 Non furnishing of BG

Circular No.76/99-Cus dated 17 November 1999 enjoined on the STP/EHTP units to execute a single B-17 bond or BG to the extent of 5 per cent of value of bond.

A unit M/s. CMC Limited, under the jurisdiction of STPI Hyderabad, had not furnished the required BG for a value of Rs.1 crore (5 percent of bond value of Rs.20 crore).

Audit pointed this out in March 2003, reply was awaited (February 2004).

2.9.6 Non revalidation of BG

Test check of records revealed that a unit of STPI Noida and three of Hyderabad had not revalidated BGs as detailed below:

(Rupees in lakh)

Name of the STPI	No. of units	Total BG Value	Date from which not revalidated
Noida	1	25.00	12.01.2003
Hyderabad	1	25.26	24.09.1999
Hyderabad	1	121.10	2001
Hyderabad	1	3.25	25.10.2000

This was pointed out in May 2003, STPI Noida replied (February 2003) that action would be taken to get them revalidated. In other cases reply was awaited (February 2004).

In addition, another unit M/s. Wipro Technologies (STPI Hyderabad) had furnished BG which was less to the tune of Rs.70.17 lakh (5 per cent of bond value of Rs.17.96 crore being Rs.89.83 lakh and BG furnished being only Rs.19.65 lakh). BG was prescribed to secure interest of government in case of misuse or failure of fulfilment of conditions of notification and Exim Policy. However, in the above cases safeguards had not been put in place.

On this being pointed out, it was replied (June 2003) that action would be taken to get them revalidated.

2.10 De-bonding

2.10.1 Delay in de-bonding of non operating units

According to Customs notification dated 22 October 1991 only such goods which are required for the purpose of development of software are eligible for duty exemption with EO period and bonding period of the STP unit being five years.

Audit scrutiny revealed that three units M/s. Banyan Network Private Limited, M/s. Impel Software Solution Limited and M/s. Digital Studios Private Limited, (STPI Chennai) had imported capital goods for a total value of Rs.4.45 crore. The units had not commenced commercial production and the capital goods imported duty free were lying idle for more than five years. The Director STPI had failed to take penal action or to de-bond the non operating units under condition No.4 of monitoring guidelines even after five years. Since, the units had not utilised the duty free imported capital goods, duty foregone of Rs.2.77 crore and interest amounting to Rs.2.11 crore were recoverable, besides penalty.

On this being pointed out in June 2003, STPI Directorate Chennai replied that, action was initiated to issue show cause notices to the units.

2.10.2 Non-execution/delay in execution of LUT

According to the provisions of paragraph 9.6 of Exim Policy 1997-2002, every STP/EHTP unit was required to execute an LUT[4] with Director, STPI in the prescribed proforma. Similarly, in the event of revision of LOP a supplementary LUT was to be executed by such STP/EHTP unit. In the event of failure to execute such a supplementary undertaking/agreement, the modified/enhanced benefits would not be applicable to the concerned unit.

Fourteen units of STPI Hyderabad, and two units of STPI Pune, which were granted extensions on the expiry of initial bonding period had not executed the supplementary legal agreements in violation of the Exim Policy conditions. One unit under STP, Kolkata had delayed renewal of their LUT with STPI for three months and another unit whose agreement was due for renewal on 7 October 1999 had not done so whereupon their registration was cancelled on 19 July 2000. The unit was subsequently recommended for de-bonding by STP, Kolkata on 4 February 2003 after 40 months of expiry of registration period in October 1999. The unit had also not renewed its private bonded warehouse cum manufacturing licence since 31 December 1999.

On this being pointed out in November 2002, STPI Hyderabad admitted the audit observation (August 2003) and stated that legal agreement was since being executed by the units with retrospective effect and reply in other cases was awaited (February 2004).

2.11 Monitoring

The overall responsibility of administering the scheme lies with the Department of Electronics (DOE). According to monitoring guidelines, the performance of STP/EHTP units

[4] Legal undertaking

have to be jointly reviewed by the Director of STPI and concerned Customs/Central Excise officers in the presence of representatives of the units on six monthly basis i.e April - September each year on the basis of quarterly performance reports/annual performance reports furnished by the units. Based on this joint review Director STPI/DOE are to prepare a report for information of the Department of Commerce and Central Board of Excise and Customs and suggest corrective measures to enable defaulting units to fulfill their obligations according to Exim policy/customs notifications. Customs department is to initiate action on the basis of the report for demanding duty with interest for not fulfilling conditions of customs notifications and Director of STPI have to forward the case of defaulting unit to DGFT to take penal action for non fulfilment of conditions of Letter of Approval under FT (D&R) Act 1992.

However, several shortcoming in this regard were noticed:

2.11.1 SCN to defaulting units not issued

According to para 3-IV of appendix 16-E of HBP Vol. I 1997-2002 of the guidelines issued by the Ministry of Commerce for monitoring the STP/EHTP scheme, if the unit fails to earn the prescribed EO/NFEP continuously for three years, Director STPI is required to issue a show cause notice to the units indicating the shortfall in earning foreign exchange with a direction to set right the short fall in subsequent years.

Test check of records revealed that nine units, (STPI Chennai) had not achieved the positive/minimum EO/NFEP continuously for three years from the date of commercial production (2000 –2001) even though they had imported capital goods worth Rs.11.43 crore with duty foregone amount of Rs.4.56 crore. However, no show cause notice was issued by the Director STPI.

This was communicated to Director STPI Chennai (June 2003), whose reply was awaited (February 2004).

2.11.2 Separate accounts for STP units not maintained

According to para 160 and 9.4 of HBP Volume I (1992-97 and 1997-2002), respectively if an enterprise is operating both as an STP and EHTP unit, two distinct identities with separate accounts are to be maintained to distinguish imports and exports or supplies effected by such STP units from those made by the other units of the enterprise.

Audit noticed that a unit, M/s. Indotronix Computers Private Limited, (STPI Hyderabad), was permitted to operate as an STP unit under STP complex (July1991). This enterprise was already operating another unit outside the scheme since 1987 with the same legal identity. Although both the units were operating concurrently from July 1991, separate accounts to distinguish exports or supplies of both units were not maintained. An attempt to reconcile the export figures shown in Annual Performance Report of STP unit with those of combined Balance Sheets revealed that the export performance was incorrectly shown higher than the actual for the period ended March 1995 and 1998. But it was certified (February 2003) by the STPI that the said unit had fulfilled its EO. In view of unreliability of the figures and absence of proper accounts, it was not clear how the STPI had satisfied itself regarding the fulfilment

of the EO by the unit. As a result the fulfilment of EO by the STP unit could not be ascertained.

2.11.3 Non furnishing of performance reports

According to terms and conditions stipulated in the LOP and LUT read with para 9.11 of HBP Vol.I (1997-2002) each STP/EHTP unit is required to furnish performance reports in the prescribed proforma.

Test check of records revealed that, in STPI Hyderabad, 1107 units and in STPI Bangalore 25 units had failed to furnish performance reports. As a result, the correctness of achievement or shortfall in EO/NFEP could not be monitored by the STPI.

On this being pointed (May 2003), Director STPI Hyderabad stated (August 2003) that all registered units would be asked to furnish the annual performance reports immediately. In other cases reply was awaited (February 2004).

2.12 Non recovery of Service Charges

In accordance with para 8 relating to service charges of STPI, (Hand book on STPI Scheme) each STP unit is required to pay annual service charge to STPI Director as per the following norms:

1. Export upto Rs.50 lakh — Rs.15,000 per annum
2. Export above Rs.50 lakh but upto Rs.300 lakh — Rs.50,000 per annum
3. Export above Rs.300 lakh — Rs.1.00 lakh per annum

Test check of records revealed that service charges to the tune of Rs.2.77 crore were not realised by the STPI Directorates as detailed below:

(Rupees in crore)

Sl. No	Name of the STPI	No. of units	Amount
1	Chennai	30	0.98
2	Kolkata & Bhubaneswar	15	0.02
3	Bangalore	178	0.71
4	Hyderabad	43	0.14
5	Noida	112	0.59
6	Trivandrum	14	0.33
	Total	**392**	**2.77**

On this being pointed out in June 2003, Director STPI Hyderabad stated (August 2003) that efforts were being made to recover the outstanding dues. The reply in other cases was awaited (February 2004).

2.13 Conclusion

Lack of proper monitoring by the Department provided an opportunity to the defaulter units to misuse provisions of Exim policy and customs notifications. Various departures from stipulated provisions brought out in the review highlight the need for better coordination between Ministry of Finance, Ministry of Communication and Information Technology as well as Ministry of Commerce to tighten controls and exercise stricter vigilance over the STPs to ensure that such benefits provided under the STP scheme are not used by the units only for their own good.

The review report was forwarded to the concerned Ministries in October 2003, whose replies were awaited (February 2004).

CHAPTER III: WORKING OF INLAND CUSTOMS BONDED (PUBLIC/PRIVATE) WAREHOUSES

3.1 Highlights

- **Non observance of the provisions of the Customs Act, 1962 and instructions issued by the Ministry resulted in excess holding of goods in warehouses, improper control, non submission of bonds, non receipt of re-warehousing certificates and non realisation of customs share, involving revenue of Rs.4477.06 crore.**

(Paragraph 3.4, 3.6, 3.7, 3.10 & 3.19)

- **Goods worth Rs.206.88 crore involving duty of Rs.185.34 crore were not sufficiently safeguarded through insurance policies.**

(Paragraph 3.5.1)

- **Loss of revenue of Rs.50.38 crore occurred due to theft, shortage, irregular extensions/relinquishment of title to goods after warehousing and postponement of clearance of warehoused goods.**

(Paragraph 3.5.2, 3.8.1, 3.8.2 & 3.8.3)

- **Non/short recovery of revenue amounted to Rs.9.48 crore on account of duty and interest on irregular clearance/removal of warehoused goods.**

(Paragraph 3.11 & 3.12)

- **Non/delayed disposal of uncleared goods and non restriction of warehousing period for perishable goods led to blockage of revenue of Rs.536.82 crore and loss of revenue of Rs.16.27 crore. Age analysis of 2860 cases involving blockage of revenue of Rs.387.14 crore revealed that 65 per cent of revenue was blocked for more than 5 years and 29 per cent for over 10 years.**

(Paragraph 3.8.4, 3.13, 3.14, 3.15, 3.16 & 3.17)

- **Non recovery of duty on shortages of liquid cargo clearance involved revenue of Rs.13.25 crore.**

(Paragraph 3.9)

3.2 Introduction

Warehousing is a facility allowed to importers to defer payment of duty on imported goods for a period permissible under the Customs Act, 1962 till their actual clearance on payment of appropriate duty or their re-export without payment of duty to a foreign port or their removal

to other warehouses or their supply to foreign going vessel or aircraft as provision or store. The statutory provisions of warehousing are contained in sections 57 to 73 of the Customs Act, 1962.

3.3 Audit Objectives

Records for three years from 1999-2000 to 2001-2002 maintained in Custom houses relating to 92 public and 250 private bonded warehouses appointed/licenced by Customs and Central Excise Department in 37 Commissionerates were examined during August 2002 to June 2003 with the objective of seeking assurance that:-

(i) the rules, regulations and procedures framed under the Customs Act were being followed scrupulously during warehousing and clearance of goods,

(ii) timely and effective action was being taken in the case of time expired uncleared goods and

(iii) Internal controls and monitoring mechanism were firmly in place to ensure check on misuse of the facility.

Audit findings are contained in the succeeding paragraphs.

3.4 Excess holding of goods in warehouse

Public bonded warehouses are appointed under section 57 while private bonded warehouses are licenced under section 58 of Customs Act, 1962. At the time of grant or renewal of a licence, the maximum stock in terms of value of goods and duty that can be stored in the warehouse are specified in the licence by the Customs department, wherein it is stipulated that the value of goods stocked in the warehouse and duty thereon should not at any point of time exceed the ceilings specified.

Test check revealed that in 23 cases of four Commissionerates, excess stock worth Rs.39.50 crore was held. In another case (Bangalore) goods involving duty of Rs.21.06 lakh were kept in the warehouse without a valid licence during August 2000 to November 2001.

3.5 Insufficient insurance coverage of warehoused goods

According to guidelines issued by Ministry of Finance, Department of Revenue in Circular No.99/95 dated 20 September 1995 for private warehouses, warehoused goods are to be insured by the warehouse keeper against theft, pilferage, fire, accidents, other natural calamities, risk against rioting etc at least for a value equal to the customs duty by a comprehensive insurance policy drawn in favour of the Commissioner of Customs. Similar guidelines for safeguarding revenue in respect of public warehouses were not in existence except for a clause in the appointment/renewal of licence to the effect that the licence holder would be solely responsible for the safe custody of the bonded goods.

3.5.1 Audit scrutiny revealed that in 84 warehouses (49 public and 35 private) in 13 Commissionerates there had been violations in this regard. In 43 warehouses (34 public and 9 private) insurance policies of only Rs.73.66 crore were taken and were woefully insufficient

to safeguard duty amount of Rs.144.33 crore. Duty of Rs.41.01 crore involved in 32 other warehouses (15 public and 17 private) was not covered at all by any policy and in nine other private warehouses the policies were not drawn in favour of Commissioner of Customs but in favour of warehouse keepers.

Illustrative cases are narrated below:-

(a) In a public bonded warehouse under Hyderabad-II Commissionerate insurance of Rs.3 crore was recovered from insurance company. Central Warehousing Corporation had requested permission of Customs Department (December 2001) to remit the amount of Rs.3 crore to the importer towards CIF value of goods damaged in flood but the customs duty of Rs.3.18 crore remained unprotected and unrealised besides notional loss of interest of Rs.1.63 crore.

(b) In a public bonded warehouse at Howrah industrial area, the fire insurance policy covering Rs.10 lakh expired in January 1998. In April 1998 a fire broke out and goods involving duty amounting to Rs.3.39 crore were destroyed. The warehouse keeper disowned any liability for payment of customs duty when demand was raised after a year (May 1999) and no recovery could be made. There was no reply forth coming on why the demand had been raised after a year of the fire or why only a small portion of the amount had been covered in insurance.

(c) In respect of a private bonded warehouse under Thiruchirappally Commissionerate, the customs duty on stock held in the warehouse as on 22 February 2002 was Rs.54.81 lakh against the insured value of Rs.40 lakh resulting in inadequate insurance coverage and consequent risk of loss of duty. This was pointed out in June 2003, reply was awaited (February 2004).

3.5.2 Loss due to theft, shortage etc.

Test check of records in three Commissionerates revealed that in 219 cases in nine warehouses, due to inadequate provision for safeguard by the warehouse keepers according to instructions ibid, loss of revenue of Rs.15.67 crore occurred owing to theft, pilferage, burglary and shortage of goods.

3.6 Improper control over warehoused goods

Provisions of section 62 of the Customs Act, 1962 read with provisions of Customs Manual stipulate that warehoused goods cannot be removed from the warehouse without the permission of proper officer. Preventive officer of customs is to accompany the importer/agent with the key of customs lock and is to put his signature in the bond stock register maintained in the warehouse. The private warehouse keeper has to submit statement report of receipt, issue, balance in bond to customs bond department to locate time expired goods lying in warehouses and to ensure that there is no discrepancy in the stock of Custom house record vis-à-vis warehouse record.

3.6.1 Non authentication of into bond bills of entry/ex-bond bills of entry

Scrutiny of warehouse stock registers maintained under 11 Commissionerates revealed instances of non-attestation of entries relating to 763 into bond bills of entry and 2029 ex-

bond clearances involving duty of Rs.2094.26 crore/Rs.2094.27 crore respectively. In the absence of any indication in the registers, of bond superintendents having checked the entries once a month, it is not known how the Department guarded against the risk of substitution of warehoused goods and their unlawful removal.

A few cases are mentioned below:-

(a) Substitution of imported goods in 39 bonds involving duty of Rs.4.77 crore imported through Chennai Air Commissionerate during 1995 to 1998 came to light only in October 1999 indicating that the Custom house failed to prevent misuse of the warehousing facility by timely detection.

(b) Picture tubes having assessable value of Rs.37.38 lakh with duty involvement of Rs.25.08 lakh were warehoused in Central Warehousing Corporation (CWC) at Madhavaram. The bond officer had not signed the warehouse register against entries of into-bond and ex-bond clearances. Similar was the fate of tele equipments having assessable value of Rs.66.57 lakh with duty involvement of Rs.35.82 lakh in CWC at Ambattur.

3.6.2 In two Commissionerates of Kolkata and Delhi, 106 consignments of liquid cargo valued at Rs.1126.44 crore involving duty of Rs.125.04 crore were removed without due authorisation by the customs authorities.

3.6.3 To curb the trend of inordinate delay in clearing warehoused goods, Hyderabad Customs Public Notice No.38/89 dated 25 May 1989 denied warehousing facility to those importers whose goods were lying uncleared in the warehouse after expiry of warehousing period. Contrary to this M/s. Malavika Steel Limited (Kolkata) was allowed to warehouse the goods in the customs bonded warehouse despite the fact that the firm failed to clear 15 consignments of goods warehoused between 1995 and 2000 valued at Rs. 34.86 crore with customs duty of Rs. 15.38 crore and interest of Rs. 15.65 crore thereon.

3.7 Non submission/deficient warehousing bond

According to section 59 of Customs Act, 1962, the importer warehousing the goods is required to execute a bond binding himself to a sum equal to twice the amount of the duty assessed on such goods. Further, according to provisions of section 73 of the Act, these bonds are to be cancelled when all amounts due have been paid or the goods are duly accounted for.

Audit scrutiny of records in four Commissionerates revealed 74 cases in respect of which bonds for Rs.10.12 crore only against the required bonds at twice the amount of duty worth Rs.33.84 crore, were executed.

In New Custom house, Delhi and Inland Container Depot (ICD) Gurgaon, 689 bonds for Rs.195.30 crore executed during May 1997 to March 2001 were lying un-cancelled due to non compliance of provisions of section 73 ibid by the Customs Department. On this being pointed out, the ICD Gurgaon cancelled all the 24 bonds of Rs.10.62 crore.

3.8 Irregular extension of warehousing period

According to section 61 of Customs Act, 1962, the warehousing period prescribed is one year initially subject to its being extended by the Commissioner of Customs up to six months, and by the Chief Commissioner of Customs for a further period as he may deem fit. The application for such extension is to be made in the prescribed format at least 15 days prior to the expiry of warehousing period, but there is no time limit for extension prescribed for Chief Commissioner.

In case of perishable goods, Commissioner of Customs may reduce the period of warehousing to 45 days or to such shorter period, as he may deem fit. Further, Ministry of Finance in their Circular F.No.473/77/89-Cus VII dated 9 October 1989 decided that extension of warehousing period should not be granted on the ground of financial constraint. In addition, it was also required that extensions should not result in loss of revenue.

3.8.1 Loss of revenue due to irregular extensions

Audit scrutiny in seven Commissionerates revealed that, in 964 cases extensions were either granted on grounds of financial constraints of the importers, or allowed for perishable goods in contravention of instructions without anticipating the loss of revenue amounting to Rs.6.67 crore as a result of deterioration of goods and reduction of duty rates.

Illustrative cases are narrated below:-

(a) A manufacturer of commercial vehicles, M/s. Hindustan Motors (Kolkata), imported gear box assembly comprising 19 packages valued at Rs.42.34 lakh and warehoused the same (February 2001) in its Customs bonded warehouse, out of which 16 could not be cleared within the permitted warehousing period, which expired in February 2002. The Commissioner granted extension in May 2002 on an application of financial hardship for six months even though the basic customs duty had been reduced from 35 per cent to 30 per cent in the interim. As a consequence of extension there was loss of revenue to the extent of Rs.2.15 lakh on clearances made between May and August 2002.

(b) Relinquishment of title to goods under section 23 (2) after initiation of proceedings for recovery of duty under section 72 of Customs Act

Consequent on the recommendation of the Public Accounts Committee in para 22 of their seventh report (Ninth Lok Sabha 1991-92), on paragraph 1.41 of the Audit Report for the year 1985-86 on Revenue Receipts Indirect Taxes-Customs, section 23 (2) of the Customs Act was amended with effect from 23 May 1994 and accordingly the relinquishment of title of goods after warehousing was not permissible.

Audit scrutiny revealed that 931 bonds were executed by Air India between September 1975 and November 1996 for warehousing of goods worth Rs.1.76 crore such as adhesive, sealants, chemicals imported under section 85 of the Customs Act, though the shelf life of the goods had expired, and permission for destruction was sought by the importer in March 2000. Despite this, Customs allowed extension upto 31 March 2002 in August 2001. Air India did not accept (October 2001) the applicability of demand notice issued under section 72 ibid

(September 2001) as the extension was valid upto 31 March 2002. The Department stated (June 2003) that matter had been referred to tax recovery cell and action under section 142 would be taken as a last resort for recovering Government dues.

In their later reply (September 2003), department stated that even in cases where demand is made by the Department under section 72 (i) (b) of the Act, it is open for the importer to relinquish title to the imported goods provided a clearance for home consumption has not been given by Customs Department. The reply of the Department was not tenable as the provisions of section 23 (2) ibid do not permit the importer to relinquish the title to goods after warehousing. Thus the duty amounting to Rs.1.10 crore was recoverable besides interest of Rs.2.27 crore.

3.8.2 Non recovery of interest on subsequent extensions

Circular No.47/2002 dated 29 July 2002 issued by the Central Board of Excise and Customs (CBEC) stipulated that it should be ensured by the Custom houses that interest accrued on duty payable on goods in the preceding period is paid by the applicant before further extension is permitted. M/s. Bellary Steels and Alloys Limited, (Mangalore Commissionerate) imported capital goods worth Rs.57.01 crore under Export Promotion Capital Goods (EPCG) Scheme and warehoused the goods under 11 bonds between September 1998 and October 2000. After completion of the initial warehousing period, the Department has allowed extensions from time to time with the latest application of February 2003 for extension upto 13 December 2003 pending with Chief Commissioner of Customs and Central Excise, Bangalore.

Grant of extension without recovery of interest led to interest of Rs.24.65 crore becoming payable as on 31 March 2003, besides postponement of duty amounting to Rs.30.29 crore for more than five years. Retention of capital goods for 3 to 5 years in the warehouse also defeated the purpose of imports under EPCG Scheme.

3.8.3 Postponement of clearance for availing exemption under export promotion schemes

In 15 cases of Kolkata Customs, extensions were granted on the grounds of financial crisis. In the meanwhile the importers had managed to obtain licences under export promotion schemes and availed exemption from payment of duty under Duty Exemption Entitlement Certificate (DEEC), Advance Licence and Duty Entitlement Pass Book (DEPB), and obtained duty free replenishment certificate licences, after expiry of initial warehousing period resulting in loss by way of foregoing of duty amounting to Rs.2.52 crore alongwith interest of Rs.0.88 crore thereon.

3.8.4 Non restriction of warehousing period for perishable goods

Audit scrutiny revealed 334 cases in nine Commissionerates where goods of perishable nature like paper, electronic goods, liquor, fruit juice, confectioneries, cigarette, batteries, polyester/nylon yarn and chemicals etc. with assessable value of Rs.26.95 crore were lying uncleared/undisposed of in the warehouses for periods ranging from 3 months to 25 years.

The Department had not restricted the period of warehousing according to aforesaid provisions of the Customs Act. With the passage of time the goods were losing their commercial value and a considerable amount of revenue in the form of customs duty of Rs.19.24 crore was also blocked besides loss of interest of Rs.18.40 crore.

3.9 Warehousing of liquid cargo in bulk

According to instructions of CBEC, in case of imports of bulk liquid cargo whether for home consumption or for warehousing, the shore tank receipt quantity is to be taken as the basis for levy of customs duty. For the shortages noticed between ship's load port ullage quantity or bill of lading quantity, and ullage survey report at the port of landing, the owner of the ship would be held responsible, and shall be liable to pay penalty not exceeding twice the amount of duty that would have been chargeable for shortages under section 116 of the Customs Act, 1962. However there is no provision for recovery of duty on shortages between the quantity of ullage survey report at the port of landing and quantity of shore tank receipt. In case of bulk cargo which is discharged directly through pipelines under white bill of entry without being warehoused in the shore tank, assessment of duty is to be done according to ship's ullage survey report at the port of discharge.

3.9.1 Non recovery of duty from importers on account of shortages

(a) Scrutiny of records of private bonded warehouse of M/s. Indian Oil Corporation Limited (IOCL) {Chennai (Sea) Commissionerate} revealed shortage of 2008.487 MT of bulk cargo of mineral oil on clearance made between January 1999 and August 2000 arising out of difference between the quantity received at the shore tank and the quantity cleared through ex-bond bill of entry and as such the importer was liable to pay the duty amounting to Rs.97.28 lakh. On this being pointed out in June 2003, there was no reply from the Department.

(b) Further, a private importer M/s. Hindustan Lever Limited, imported crude palmolein in December 2001 through Trichy Commissionerate. Scrutiny in audit revealed that there was shortage of 281.165 MT which could not be accounted for to the satisfaction of the proper officer and as such the importer was liable to pay the customs duty of Rs.27.72 lakh. Demand notice was issued for only Rs.4.72 lakh. Department had not replied on this being brought to their notice.

3.9.2 Non-provision for recovery of duty on account of shortage between ullage and stored quantity

In 306 cases of imports of mineral oil by M/s. IOCL through Chennai (Sea) and Kolkata Customs, shortage of 102381.459 MTs was noticed between the quantity of ullage survey report at the port of landing and quantity of shore tank receipt. The duty would amount to Rs.12 crore but there was no provision to recover duty in such a situation. Hence Rs.12 crore remained unrealised.

3.10 Non-receipt of re-warehousing certificates under section 67 of Customs Act

According to section 67 read with notification No.59-Cus dated 1 February 1963, if the warehoused goods are removed from one warehouse to another, in a different town for re-warehousing, the importer should execute a bond and give bank guarantee, binding himself to produce within 3 months or within the extended period, a certificate issued by the proper officer that the goods have arrived at the place of destination, failing which the bond equal to the amount of import duty leviable on such goods shall stand forfeited.

Test check revealed that in nine Commissionerates in 686 cases warehoused goods worth Rs.116.54 crore had been removed to warehouses in different towns, during the period May 1998 to April 2002. Neither had re-warehousing certificates been produced so far by the proper officer nor had the Department taken action to forfeit the outstanding bonds/bank guarantees. Customs duty amounting to Rs.68.92 crore involved in these cases remained unrealised.

3.11 Non levy/short levy of duty on clearance of warehoused goods for home consumption

According to section 15(i)(b) of the Customs Act, 1962, the date relevant for determination of rate of customs duty in case of warehoused goods cleared within permissible warehousing period, is the date of their actual removal from the warehouse. Further, the Supreme Court in the case of Kesoram Rayon vs Collector of Customs {1996(86) ELT 464(SC)} has held that in cases where the goods have been allowed to be cleared after expiry of the warehousing period, the removal of goods should be treated as "improper removal" and the rate of customs duty payable should be the rate prevalent on the date when warehousing period including permitted extension came to an end.

Audit scrutiny revealed 110 cases in eight Commissionerates where the goods were cleared within the permissible period but due to incorrect application of rate of duty, non levy of special additional duty, misclassification, under valuation, incorrect exemption and improper accountal of goods, customs duty amounting to Rs.2.41 crore was either not levied or levied short. Besides interest of Rs.14.48 lakh in four cases was also recoverable. On this being pointed out, the Department reported recovery of Rs.0.12 lakh in one case.

In 15 other cases (six Commissionerates) the goods were cleared after expiry of permitted warehousing period. Non application of rate of duty prevalent on the date of expiry of warehousing period resulted in short payment of duty amounting to Rs.72.93 lakh. Besides interest of Rs.1.69 lakh in four cases was also recoverable.

A few cases are narrated below:-

3.11.1 In the case of ex-bond clearance made by M/s. Caterpillar India (Private) Limited, (Chennai Commissionerate-II) availing project import concession, the warehousing period expired on 7 June 2001. No extension of warehousing period was obtained. However, the goods having assessable value of Rs.1.41 crore were allowed to be cleared on 11 July 2001 at concessional rate of duty instead of at the duty chargeable on the date on which the permitted period expired leading to short collection of duty of Rs.57.62 lakh.

3.11.2 A consignment of 25000 MT Coal imported (June 1996) by M/s. India Cements Limited, through Coimbatore Custom house was warehoused at a private bonded warehouse under the jurisdiction of Erode Central Excise Division who cleared a quantity of 24020.65 MT (February 1997 to August 1997) on payment of duty and the balance quantity of 979.35 MT had not been accounted for to the satisfaction of proper officer. Customs duty amounting to Rs.4.96 lakh was thus recoverable besides interest of Rs.6.65 lakh.

3.12 Non levy/short levy of interest on clearance of warehoused goods

According to provisions of section 61 of the Customs Act, 1962, interest is leviable at the rate fixed by CBEC within the limit of rates specified under section 47 of the said Act, on the duty payable on warehoused goods cleared after specific period of time. The interest free period of one year was reduced to six months vide notification No.30/99-Cus (NT) dated 12 May 1999, which was further reduced to 30 days vide notification No.23/2001-Cus (NT) dated 22 May 2001 read with Kolkata Customs P.No.40/2001 dated 13 September 2001 effective from 1 June 2001. The rate of interest was increased from 20 per cent to 24 per cent vide notification No.10/2001 (NT) dated 1 March 2001 effective from 16 March 2001.

Test check of records in 26 Customs and Central Excise Commissionerates separately revealed 2461 cases of ex-bond clearances during the period from 1999 to 2002 involving non levy/short levy of interest amounting to Rs.6.18 crore. On this being pointed out, the Department reported recovery of Rs.2.37 crore.

A few cases are as follows:–

3.12.1 According to circular letter dated 27 December 1993, waiver of interest on customs duty on the imports of goods related to ship building industry is allowable in view of long production programme or prolonged nature of activity of the importer.

In the case of M/s. Chowgule and Company, Goa, steel plates imported for manufacture of vessel, were warehoused in August and October 1993. According to agreement signed by the company in July 1996 the manufacturing activity commenced from 9 August 1996. The goods were de-bonded on 8 November 2000 and the payment of interest amounting to Rs.70.44 lakh on customs duty was exempted from the date of expiry of initial warehousing period till the date of de-bonding vide Ministry of Finance letter dated 3 March 2003.

Since the goods were procured and warehoused nearly 3 years before their actual requirement the exemption was not justified on the grounds of public interest and circumstances of an exceptional nature, and the reason for waiver of interest was also not specified in the aforesaid letter. The waiver of interest on the above goods upto 8 August 1996 amounting to Rs.19.77 lakh was therefore not in order.

Reply of the Department was awaited (February 2004).

3.12.2 Notification No.28/2002 Customs (NT) issued on 13 May 2002 which specified the rate of interest at 15 per cent for the specific purpose of section 47 of Customs Act 1962 was not applicable in respect of goods warehoused under section 61. Instead notification No.10/2001 Customs (NT) specifying the rate of 24 per cent per annum was applicable.

Incorrect application of rate of interest at 15 per cent instead of 24 per cent resulted in short/non levy of interest of Rs.41.29 lakh in 1068 cases in two Commissionerates of Custom, Kolkata Port and Airport.

3.13 Time expired un-cleared goods awaiting disposal action

According to section 61 (b) of the Customs Act, 1962, warehoused goods may be left in the warehouse in which they are deposited for a period of one year or such extended period as the Commissioner of Customs or the Chief Commissioner of Customs may allow. If the warehoused goods are not removed within the prescribed period, the proper officer has to demand full amount of duty chargeable on account of such goods together with all penalty, rent, interest and other charges payable in respect of the goods and the importer shall pay the demand and clear the goods. In case of failure to pay the amount demanded, the importer is liable for recovery action under section 142 ibid. Besides, the Assistant/Deputy Commissioner of Customs is required to immediately proceed to detain the goods and take action for recovery of duty by auctioning the goods according to the provisions of section 72 of the Customs Act, 1962.

Test check of records in 25 Commissionerates revealed that 3190 cases of time expired warehoused goods worth Rs.429.32 crore were awaiting disposal action for a period ranging upto 45 years from the date of expiry of warehousing period as of December 2002/March 2003. Customs duty involved in these cases amounting to Rs.247.47 crore and interest amounting to Rs.209.98 crore was recoverable. With the passage of time the goods were losing their commercial value and a considerable amount of revenue had also been blocked in the form of customs duty and interest thereon. On this being pointed out, the Department reported recovery of Rs.58.12 lakh.

Age wise analysis of un-disposed goods

Of the aforesaid time expired goods, age-wise analysis of 2860 cases involving revenue of Rs.387.14 crore awaiting disposal action in 22 Commissionerates tabulated as under, revealed that more than 65 per cent of revenue was blocked for more than 5 years, 29 per cent was blocked for over 10 years. Earliest pendency was of 45 years in Kolkata.

(Rupees in crore)

Years	No.of cases	Assessable value of the goods	Duty and interest involved
More than 20	410	2.69	7.88
Between 10 & 20	912	28.36	106.64
Between 5 & 10	505	146.37	137.22
Between 1 & 5	1033	168.77	135.40
Total	**2860**	**346.19**	**387.14**

A few cases are narrated below:-

3.13.1 M/s. Standard Motors Limited, (Chennai Sea) imported parts of automobiles in 53 consignments during the period from December 1985 to July 1988 and warehoused them in

their private bonded warehouse at Perungalathur. The company became defunct and the warehoused goods were not cleared. Customs duty involved in this case worked out to Rs.10.01 crore and interest upto the period of 31 December 2002 worked out to Rs.31.42 crore. Custom house has taken no action to realise customs duty.

3.13.2 M/s. Bafna Spinning Mills and Exports Limited, (EOU), Coimbatore imported humidification plant during March 1996 but did not file the bill of entry. Instead financier of the importer viz. M/s. Bank of Madura (Now ICICI Bank) came forward and filed the bill of entry for warehousing in the hope of finding another buyer for the imported goods, which have not so far been cleared and customs duty of Rs.1.21 crore besides interest of Rs.1.07 crore accrued upto 31 December 2002, stand unrealised.

3.13.3 M/s. Aditya Horologicals Limited and M/s. PSI Data Systems Limited, (Bangalore) warehoused goods valued at Rs.24.12 lakh, involving a duty effect of Rs.31.27 lakh, during March 1987 and June 1989. The goods were not cleared within prescribed warehousing period of one year. Extension of time was also not sought for by the importers. Thus, the revenue of Rs.31.27 lakh in both the cases remained unrealised for over a period of 10 to 12 years.

3.14 Goods pending clearance under section 49 of Customs Act

Thirteen consignments with assessable value of Rs.2.05 crore and involving duty of Rs.0.85 crore warehoused during 1995 to 2001 under section 49 of the Customs Act, 1962, in two public warehouses of Delhi Commissionerate, were awaiting clearance. With the passage of time these were losing their commercial value and also blocking Government revenue amounting to Rs.0.85 crore. Though these goods were mentioned in the monthly statements of time barred goods furnished by the custodian to the Customs Department yet no disposal action was taken by the Department according to section 48 of Customs Act.

3.15 Abandonment of warehoused goods

In four Commissionerates (Chennai Sea, Air, C EX-II and Trichy) even though detention notices had been issued (July 2002 to January 2003) in respect of 35 abandoned consignments valued at Rs.2.65 crore involving duty of Rs.1.23 crore and interest of Rs.0.25 crore, no action had been taken to dispose of the goods by way of sale or auction to realise the revenue due to the Government.

3.16 Loss of revenue due to delay in auction/sale of uncleared goods

In the case of non clearance of warehoused goods within the permitted period, without prejudice to any other mode of recovery for the realisation of duty and other charges, the proper officer may cause to detain and sell the goods to realise the customs duty and interest under Section 72 of the Customs Act, 1962.

Test check revealed that in the case of 69 consignments of goods imported through eight Commissionerates and warehoused in public and private customs bonded warehouses during the period 1987 to 2000, the importers failed to clear the goods and as such the Department detained the same and sold them through auction. With the passage of time the goods lost

their commercial value and the amount of only Rs.2.58 crore could be realised through auction against duty and interest of Rs.18.85 crore.

3.17 Blockage of revenue on closure/de-bonding of warehouses

According to provisions of section 61 of Customs Act, 1962, when the licence for any customs bonded warehouse is cancelled, the owner of the goods shall remove the goods for exportation or home consumption within seven days from the date on which notice of such cancellation is given or within such extended period as the proper officer may allow, failing which the proper officer under section 72 ibid may demand full amount of duty chargeable on such goods together with penalty, rent, interest etc. If the owner fails to pay any amount demanded, the proper officer may detain the goods and sell the goods to realise Government revenue.

Test check of records of three Commissionerates (Chennai Sea, Visakhapatanam CE-I and Delhi) revealed that three warehouses were de-bonded as early as during 1996, 1999 and 2002 but 64 consignments of warehoused goods were not cleared from the warehouses which included 17 items worth assessable value of Rs.18.08 crore involving duty of Rs.11.67 crore and interest of Rs.26.45 crore. Records and details of assessable value, duty and interest involved in the remaining 47 consignments were not furnished by the Department despite repeated requests.

In two other cases even though the duty was recovered on clearance of the warehoused consignments during 2002, the interest of Rs.1.28 crore was still recoverable.

Non initiation of action under section 72 ibid by the Department against these de-bonded warehouses, thus, resulted in blockage of revenue to the extent of Rs.39.40 crore.

3.18 Non recovery/short recovery of establishment charges

According to regulation No.4 (v) of manufacture and other operations in Warehouse Regulations 1966, read with Ministry of Finance instructions issued in April 1991, the cost of establishment charges in respect of posts created on cost recovery basis, shall be equivalent to 1.85 times the average cost of the post i.e average pay of the post and allowances including dearness allowance and other allowances.

Test check revealed that in respect of three bonded warehouses establishment charges for the period 1998 to 2002 were not recovered/short recovered by Customs Department from warehouse keepers to the extent of Rs.21.46 lakh.

3.19 Non realisation of Customs share from the custodian

According to section 150(2) of Customs Act, 1962 read with Circular No.50/97, dated 17 October 1997, 50 per cent of sale proceeds realised by the custodian in auction in respect of unclaimed/uncleared goods should be remitted to Customs Department till finalisation of consignment-wise accounts of all auctioned goods.

The custodian of a public bonded warehouse (Hyderabad II) disposed of (March 2002) 14 consignments of unclaimed/uncleared goods on which an amount of Rs.21.86 lakh was realised. The share of the customs department at 50 per cent of the above which worked out to Rs.10.93 lakh was not, however, remitted by the custodian even after a lapse of a year. This was pointed out in September 2002, reply was awaited (February 2004).

3.20 Improper maintenance of records and lack of effective monitoring mechanism

Provisions of Ministry of Finance circular No. 52/98-Cus dated 27 July 1998, envisaged that there should be regular audit and inspection by senior officers and Custom house audit parties at least once in six months. It was also made mandatory for the warehouses to submit status reports relating to consignments pending for one year and above and cross check position in the Custom house where the warehousing bills of entry originated. Further, Customs Preventive manual prescribed that the bond superintendent should check bond stock registers at least once a month and the officers posted in private bonded warehouses were required to send every month a statement of receipts, issues and balances in bond.

Review of the procedures revealed that in most of the Commissionerates these instructions were not being followed, monitoring was weak and maintenance of records improper. Warehoused and time expired goods were un-reconciled with the records of Custom houses and there was insufficient coverage of inspection/audit by senior officers and customs audit parties. So, the Department was unable to ascertain the actual quantum of time for which expired goods were lying in the warehouses. Non-initiation of action under section 72 of the Customs Act, 1962 also resulted in blockage of large amount of Government revenue, which would inevitably turn into loss with the passage of time due to deterioration, substitution and loss of commercial value of goods.

3.21 Conclusion

The review has revealed several instances of violation of rules, regulations and procedures framed under the Customs Act relating to warehousing and clearance of goods. Unjustified extensions and lack of timely and effective action in preventing misuse of the facilities led to blockage of substantial revenue. Monitoring mechanism seemed to be weak and ineffective. Audit therefore recommends that the Department improve the compliance to rules and regulations laid down, and strengthen its internal controls.

The review report was forwarded to the Ministry of Finance in October 2003. Their reply was awaited (February 2004).

CHAPTER IV: SHORT LEVY DUE TO INCORRECT CLASSIFICATION

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

4.1 Bedding, mattresses etc.

Articles of bedding and similar furnishing stuffed with any material merit classification under Customs Tariff heading 94.04.

Mention was made in para 4.1 of Report No.10 of 2003 (Indirect Taxes-Customs) that 17 consignments of sleep pad, down comforter and pillows imported by M/s. Frontier Trading, Thane during October 2000 to December 2001 through Sea Customs Commissionerate, Mumbai were declared as magnetic accupressure treatment instruments and incorrectly classified under Customs heading 9019.10 (mechano therapy appliances) even though the invoices clearly indicated that these were items of bedding, meriting classification under Chapter 94.

The case was adjudicated by the Commissioner (Imports) Mumbai, who after scrutiny of relevant catalogues, manuals, internet information, certificates from the Ministry of Health, seized documents etc. and after giving an opportunity to the importer, came to the conclusion (August 2001) that the said goods merited classification under Customs Tariff heading 9404.29. He accordingly confirmed demand for Rs.22.49 crore for imports made between March 2000 and October 2000. However, the party had gone in appeal against this.

Further audit scrutiny revealed that seven consignments of the goods imported by the same trader M/s. Frontier Trading, Thane, during January 2002 to August 2002 were again classified as 'mechano therapy appliances' resulting in short levy of duty of Rs.3.64 crore.

On this being pointed out (April to August 2002), the Ministry stated (December 2003) that after examining all aspects of the issue including the assessment practice followed in other Custom houses in the past and all the relevant documents, the Board issued a circular No.56/2001-Cus dated 25 October 2001 clarifying that such goods are more appropriately classifiable under heading 9019.10. However, later on the basis of certain additional information including opinion of the WCO, the classification of this item has been revised and put under CTH 94.04 by the Board vide circular No.44/2003-Cus dated 29 May 2003.

The reply of the Ministry is not tenable as the circular dated 25 October 2001 was totally unnecessary since the matter had been decided by the Commissioner (Imports) Mumbai in August 2001, and the circular violated the conditions stipulated in section 151A of the Customs Act, 1962. Audit's view was vindicated by the subsequent circular No.44/2003-Cus dated 29 May 2003 classifying the said goods under Customs Tariff heading 94.04 and in direct contrast to the circular dated 25 October 2001. However, there was loss to Government revenue on imports made during the interim period.

4.2 Motorcycle and vehicle parts

4.2.1 Specially designed parts of motor vehicles i.e. 'head cylinders, block cylinders, and TM case of aluminium castings', are classifiable under Customs Tariff heading 8708.99.

M/s. Maruti Udyog Limited imported 51 consignments of specially designed parts of car namely 'head cylinders, block cylinders and TM case of aluminium castings' through ICD Tughlakabad/Garhi Harsaru under Delhi Commissionerate during February to May 2002 which were classified/cleared as 'other goods of aluminium' under Customs Tariff heading 7616.99. The imported goods were specially designed parts for specific models of motor vehicles and would thus have merited classification under Customs Tariff heading 8708.99. The misclassification resulted in short levy of Rs.2.77 crore.

On this being pointed out (June/August 2002), the Department citing CEGAT judgment dated 9 October 2001 in the case of Uni Deritand Limited versus Commissioner of Customs, Nhava Sheva, {2002 (139) ELT 586 (Tri-Mumbai)} stated (July 2002) that the items were raw castings of aluminium which could not be used as such in the engines of motor vehicles and that castings underwent 18 to 31 different stages of processing to make them suitable for use in motor vehicles, as such they were correctly classified under heading 7616.99.

The reply of the Department is not tenable in view of the Supreme Court pronouncement dated 15 January 2003 in the case of G.S. Auto International Limited versus Collector of Central Excise, Chandigarh, {2003 (106) ECR 580 (SC)} relating to classification of 'nut, bolts for motor vehicles', wherein it had been held that the true test for classification was 'the test of commercial identity and not the functional test'. The court further held that for the purpose of classification under chapter heading 87.08, the test to be applied was whether the goods were suitable for use solely or primarily with articles of chapter heading Nos. 87.01 to 87.05; if the answer was in the affirmative, the goods would be classifiable under chapter heading 87.08, while in the negative, they would have to be classified under chapter heading No.73.18. As in the instant case, the imported goods are suitable solely for cars, they would merit classification under Chapter heading No.87.08 and not under 76.16.

Reply of the Ministry had not been received (February 2004).

4.2.2 'Motorcycle parts' merit classification under Custom Tariff heading 87.14.

Thirty consignments of parts of motorcycle e.g. driven gear, gear primary driven, collar, drive gear and electrical parts imported by M/s. Hero Honda Motors Limited and two others between September 2001 to January 2003 through Custom house Delhi, were classified under Customs Tariff heading 8483.40/8504.90/8547.90 treating them as independent goods even though the imported goods were parts of motorcycles and would merit classification under Customs Tariff heading 8714.19. The incorrect classification resulted in short levy of duty of Rs.85.90 lakh.

On this being pointed out during February 2002 to March 2003, the Department stated (December 2002 to June 2003) that gears are specifically covered under Customs Tariff

heading 8483.40 and according to Note 2(e) of section XVII, the articles of Customs Tariff heading 84.83 are not regarded as parts of goods of Chapter 87 if they are integral parts of the engine.

The reply of the Department is not tenable as the goods imported were appropriately covered by the HSN explanatory General Note (III) B (1) which stipulates that the classification of a part or accessory when falling in one or more other section as well as in section XVII, would be finally determined by its 'principal use'. As the goods imported were specifically covered by the HSN explanatory note serial No.3 below heading 87.14, they merited classification as motorcycle parts.

Reply of the Ministry had not been received (February 2004).

4.3 Machineries and parts

4.3.1 'Plotters' being output units of data processing machines, transforming the data of computer aided designing/drawing into written/visual forms, are classifiable under Customs Tariff heading 84.71.

Forty one consignments of 'design inkjet plotters/colour inkjet plotters' imported by M/s. Hewlett Packard and two others through Delhi Commissionerate during February 1996 to February 2003 were classified and assessed under CTH/CETH 9017.20/90.17 as 'automatic drafting machines'. The misclassification resulted in short levy of duty of Rs.55.41 lakh. In a similar objection for a consignment of plotters imported in January 1996 by M/s. Hewlett Packard the Department accepted the classification of the goods under heading 84.71.

This was pointed out to the Department between February 1996 to February 2003; reply was awaited (February 2004).

4.3.2 'Air conditioners and parts thereof' merit classification under Custom Tariff Heading 84.15.

A consignment of complete 'air-conditioning units' for cooling crane cabin, imported in May 2001 through Custom house, Kolkata by M/s. National Aluminum Company Limited, Orissa was classified under Customs Tariff heading 8431.49 as parts of crane instead of as complete machinery under Tariff heading 84.15, which resulted in short levy of duty of Rs.13.39 lakh.

On this being pointed out (April 2002), the Department stated (July 2002) that the importer had been requested to make voluntary payment of the short levied amount as the demand was time-barred. Further progress was awaited (February 2004).

4.3.3 'Plain paper photocopier with drum' employing an indirect process for projecting optical image via an intermediate (such as selenium coated drum or plate) onto the copy as defined in the HSN explanatory note was classifiable under sub-heading 9009.12 of the Customs Tariff.

Six consignments of 'plain paper photocopier with drum accessories' imported through Customs Commissionerate (Sea), Kolkata between March 2001 and July 2002 by M/s. Kilburn Reprographics Limited, were assessed under heading 9009.11 of the Customs Tariff, treating them as electrostatic photo-copying apparatus operated by 'direct process'. In fact,

the imported goods were plain paper copiers, involving indirect electrostatic process, using selenium coated drum as an intermediate, thus meriting classification under Customs Tariff heading 9009.12. The incorrect classification resulted in short levy of duty amounting to Rs.9.68 lakh including interest.

On this being pointed out (June/July and November 2002), the Department reported (July 2003) recovery of Rs.0.46 lakh and stated that the importer had agreed to pay the short levy. Further progress was awaited (February 2004).

4.3.4 'Parts and accessories of radio cassette player' are classifiable under heading 8522.90.

Two consignments of 'parts of radio cassette player' viz. printed circuit boards, front control assembly, plastic moulded and extruded parts etc. imported by M/s. Nippon Audiotronics Limited, New Delhi in August/September 2001 through ICD, Patparganj, Delhi were classified under Customs Tariff Heading 8529.90 treating them as parts of radio telephony/radio telegraphy/radio apparatus instead of as parts of radio cassette player classifiable under heading 8522.90. The incorrect classification resulted in short levy of duty of Rs.9.53 lakh.

This was pointed out to the Department in February 2002 and August 2002; reply was awaited (February 2004).

4.4 Other cases

Seven other cases of incorrect classification of goods imported by eleven importers involving short levy of duty of Rs.36.33 lakh were reported to the Ministry. Out of these the Department admitted two cases involving Rs.8.82 lakh and reported recovery of Rs.3.04 lakh in two cases as detailed below:

(Rupees in lakh)

Sl. No.	Details of product	Name of the importers M/s.	Heading where classifiable	Heading where classified	Amount short levied	Amount admitted	Amount recovered
1	Industrial chain	NTPC Limited & Paradeep Phosphates Limited	73.15	84.31/ 84.28	7.43	7.43	1.65
2	Gear case assembly	LG Electronics & Onida Savak Limited	84.50	84.83	7.08	Not admitted	--
3	Plastic handles for refrigerators	Maharaja International Limited	84.18	39.26	7.02	Not admitted	--
4	Parts of air-conditioning system	Sandan Vikas Limited & two others	84.15	76.08	7.01	Not admitted	--
5.	Calculator rubber key pads	Ellora Times Limited	40.16	84.73	4.07	Not admitted	--
6.	Packet switch	Tata Teleservices Limited	85.36	85.17	2.33	Not admitted	--
7.	PCB for inverters	Alcatel Network System	85.04	85.17	1.39	1.39	1.39
	Total				36.33	8.82	3.04

CHAPTER V: SHORT LEVY DUE TO INCORRECT GRANT OF EXEMPTION

Short levy of duties aggregating Rs.3.65 crore in 33 cases on account of incorrect grant of exemptions were pointed out to the Ministry. Some illustrative cases are narrated below:

5.1 Incorrect application of exemption notification

5.1.1 Notification No.21/2002-Cus dated 1 March 2002 {serial No.226(A)} prescribes concessional rate of basic customs duty on import of 'machinery, instruments, apparatus and appliances required for renovation or modernisation of fertilizer plant' subject to fulfilment of specified condition.

Two consignments of 'catalyst' imported (July and August 2002) through Kolkata (Sea) Customs Commissionerate for use in the manufacture of ammonia by M/s. Fertilizer Corporation of India and M/s. Hindustan Fertilizer Corporation Limited, were assessed to duty at concessional rate under notification ibid treating it as a part of renovation and modernisation of fertilizer plants even though the catalyst, being a chemical product did not fall under the definition of the items specified in the notification. The incorrect application of exemption notification resulted in short levy of duty including interest of Rs.51.35 lakh.

On this being pointed out (January 2003), the Department admitted (June 2003) the objection and reported (June/July 2003) recovery of Rs.51.23 lakh.

5.1.2 According to notification No.20/99-Cus dated 28 February 1999 read with notification No.16/2000-Cus dated 1 March 2000, import of compact disc read only memory (CD-ROM) classified under Customs tariff chapter 85 was allowed at concessional/nil rate of customs duty.

Eleven consignments of 'compact disc recordable' (CD-R) imported during November 1999 to January 2001 by M/s. Jupiter Infosys Limited, Kolkata and M/s. Sulabh Trading Company Delhi, through Kolkata (Sea) customs were assessed to concessional/nil rate of duty even though the goods imported were not covered by the exemption notifications ibid. The incorrect grant of exemption resulted in short levy of Rs.45.08 lakh.

On this being pointed out (November 2000 and November 2001), the Department stated (May 2001) that since CD-R is a type of CD-ROM that can be written and CD-ROM is a system for recording, storing and retrieving electronic information from the compact disc, as such, the exemption granted to CD-R as CD-ROM is correct. The Department referred to the Ministry of Finance's clarification dated 26 May 1997 wherein it was stated that both recorded and unrecorded disc were covered under CD-ROM. The reply of the Department/Ministry's clarification is not tenable on the grounds that:

i) According to Encyclopedia Britannica, CD-ROMs are recorded only once, hence the tag 'read only'. On the other hand, CD-R may be written and used repeatedly by the user. Further, CD-R differs from CD-ROM in having a light-sensitive organic dye layer which can be 'burned' to produce a chemical 'dark' spot.

ii) CD-ROM has been classified under sub-heading 8524.31 as recorded media under serial No.311 of exemption notification No.21/2002-Cus dated 1 March 2002 whereas CD-R has been classified as unrecorded media under sub-heading 8523.90 in the First Schedule to the Customs Tariff Act, 1975 appended to the Customs Tariff for the year 2003-04.

Reply of the Ministry had not been received (February 2004).

5.1.3 Vide Customs notification No.21/2002 (serial No.347) dated 1 March 2002 import of 'parts of aeroplanes' required for manufacture or servicing of aeroplanes are exempt from customs duty.

Seven consignments of 'aeroplane seat & other accessories' (cushion, fairing arm cap, food tray and ash tray), 'oven' and 'DVD players' imported by M/s. Indian Airlines Limited, and two others through Custom house, Delhi and Mumbai between July 2000 and December 2002 were cleared extending benefit of notification dated 1 March 2002 even though the goods imported were not required for manufacture or servicing of aeroplanes. This resulted in non levy of duty of Rs.22.58 lakh.

On this being pointed out (July 2000 to March 2003), the Department in respect of seat accessories stated (July 2003) that according to the explanation below condition No.67 attached to the notification dated 1 March 2002, the goods imported were eligible for exemption. Further, in case of 'oven' the Department stated (July 2001) that an oven is an integral part of the aircraft. The reply of the Department is not tenable as exemption was applicable to the 'parts of aeroplane' required for manufacture or servicing of aeroplanes. CEGAT in the case of Collector of Customs vs Jolly Exports {1990 (45) ELT 612 (T)} held that in order to determine whether the subject goods are accessories or parts, the distinction had to be drawn on the basis of whether they were integral parts used for smooth and efficient functioning or not. If a machinery cannot be worked without the part, it ceases to be an accessory. In the instant case goods are not part of aeroplanes but more appropriately accessory to aircrafts.

Reply of the Ministry had not been received (February 2004).

5.1.4 According to notification No.25/2002-Cus (serial No.17) dated 1 March 2002, import of 'panel surface coating equipments' used in the manufacture of 'cathode ray tubes' is subject to concessional rate of customs duties.

A consignment of 'licenced technology for optium system CRT coating system' (used for manufacturing cathode ray tubes) imported (April 2002) by M/s. Samtel Color Limited, Ghaziabad through Custom house, New Delhi was subjected to concessional rate of customs duty under notification dated 1 March 2002, even though the item imported was not covered by the exemption notification. The incorrect grant of notification benefit resulted in short levy of Rs.13.65 lakh.

On this being pointed out in September 2002/January 2003, the Department stated (February 2003) that the imported item was technical know how essential for the proper operation of the CRT coating systems in the manufacture of cathode ray tubes, and was, as such, classifiable

as 'panel surface coating equipment' which is listed under serial No.17 of the notification dated 1 March 2002.

The reply of the Department is not tenable as exemption under the notification had been given to 'panel surface coating equipment' and not to 'licenced technology for optium CRT system'.

Reply of the Ministry had not been received (February 2004).

5.1.5 Machinery or equipment specified in list 18 A of the notification No.17/2001-Cus dated 1 March 2001 (serial No. 245A), required for textile industry is subject to concessional rate of duty. Accordingly 'fully fashioned high speed knitting machine' is eligible for benefit under the notification ibid.

M/s. Laveena Hosiery Private Limited imported 'fully fashioned high speed double head flat knitting machine', which was assessed under the notification ibid. Scrutiny of notification revealed that 'double head flat fully fashioned high speed knitting machine' was not covered by the notification. Thus, incorrect grant of exemption resulted in short levy of duty of Rs.13.28 lakh.

On this being pointed out (June 2002 and March 2003) the Department while furnishing the catalogue of the goods imported stated (March 2003) that the item imported was 'fully fashioned high speed knitting machine' and was, therefore, covered under serial No.5 of list 18 (A) of the notification.

The reply of the Department is not tenable as scrutiny of the catalogue revealed that the good imported is a computer controlled automatic three system double head fully fashioned high speed knitting machine which is not covered under aforementioned notification. The technical specifications of machines that are eligible for exemption under the said notification have been given in detail in list Nos.18 and 18(A) (serial No.6 and 7 of list 18A and serial No.42 to 68 and serial No.86 of list 18). Machines with specifications like 'double head' (mentioned in the Invoice), and computer controlled automatic three system double head (mentioned in the catalogue) are not included in list No.18/18A and therefore, not eligible for benefit under the notification ibid.

Reply of the Ministry had not been received (February 2004).

5.2 Incorrect exemption due to misclassification

'Catalytic converters' (Chapter heading 8421.29) when imported are assessable to concessional rate of duty under Custom notification No. 17/2001 dated 1 March 2001.

'Automobile components' imported by M/s. Honda Siel Cars (P) Limited (February 2002) through Delhi Commissionerate were assessed to concessional rate of duty under the notification ibid treating them as 'catalytic converters'. Audit scrutiny revealed that the imported items were components of motor vehicles (chapter heading 8708.99) and thus not

eligible for the exemption. The misclassification and incorrect grant of notification benefit resulted in short levy of duty amounting to Rs.32.40 lakh.

On this being pointed out (July 2002 and November 2002), the Department contended (February 2003) that the imported goods were 'catalytic converters' and classified correctly. The reply of the Department is not tenable because the invoice mentions the imported items as 'automobile components' and not 'catalytic converters'. Moreover, clearance through green channel was allowed to the imported goods without any physical verification, due to which specification of the goods as mentioned in the bill of entry could not be confirmed.

Reply of the Ministry had not been received (February 2004).

5.3 Condition of the notification not fulfilled

5.3.1 According to Customs notification No.16/2000 dated 1 March 2000 read with notification No.111/2000 dated 27 August 2000, crude palm oil and its fraction of edible grade, with free fatty acid content of at least 2 per cent, imported on or after 29 November 2000 are eligible for concessional rate of duty subject to fulfilment of the condition that the imported oil shall be used in the manufacture of vanaspati in the importer's factory having captive hydrogen generation facility.

Three consignments of 'edible grade crude palm oil with free fatty acid content of more than 2 per cent' imported by M/s. Bharat Margarine Limited, through Custom house Kolkata (Sea) in January 2001 were subjected to concessional rate of customs duty under notification dated 1 March 2000. However, audit scrutiny revealed that the importer had misdeclared existence of captive hydrogen generation facility in his factory at the time of import, a fact that was later accepted by him. Thus, irregular grant of exemption benefit resulted in short levy of Rs.27.57 lakh.

This was pointed out to the Department in September 2001. Reply had not been received (February 2004).

5.3.2 Vide notification No.148/94-Cus dated 13 July 1994, goods such as food- stuffs, medicine, clothing etc imported by charitable organisations as free gifts from abroad for the purpose of free distribution among the poor and needy are exempt from payment of customs duty subject to production of certificate of distribution by the importer within six months or such period extended by the prescribed authority.

Audit scrutiny revealed that the prescribed certificates of distribution against import of seven consignments of clothing through Custom house, Kolkata between January 1996 and April 1999 by Bharat Mukti Mandal, Ballabhgarh and four other charitable organisations were not produced even after expiry of the prescribed period. Duty recoverable in these cases amounted to Rs.25.94 lakh.

On this being pointed out (May 2000), the Department issued (January 2002) demand notices. Further progress was awaited (February 2004).

5.3.3 Notification No.32/97-Cus dated 1 April 1997 exempts goods imported into India from the whole of the duty of customs and additional duty under Customs Tariff Act subject to the condition that the goods are imported for execution of an export order placed on the importer by the supplier of the goods for jobbing. The goods imported including resultant products have to be re-exported to the supplier of the goods or to any other person which the supplier may specify within six months from the date of clearance or within such extended period as the Assistant Commissioner of Customs may specify. Where the goods are in the nature of patterns, drawings, jigs, tools, fixtures, moulds, tacks and instruments, they may be allowed by the Assistant Commissioner of Customs to be retained subject to payment of customs duty leviable as on the date of import without allowing any depreciation. Deviations from these provisions were noticed as below:

(a) M/s. AF Technologies Private Limited imported 'injection moulding tools' (December 1999) through Air Cargo Complex, Bangalore. The goods were cleared duty free under the Customs notification ibid. Audit scrutiny revealed that the Department had granted extension to retain the goods upto 31 December 2001, though the EO was achieved by May 2001. The importer however had not re-exported the tools after 31 December 2001 but sought extension to retain the tools in anticipation of further orders from the supplier. The retention of the tools after the permissible period without payment of duty, in anticipation of order from the supplier, was not contemplated in the notification. The Department did not start action to levy duty of Rs.13.99 lakh.

On this being pointed out between January 2001 to March 2003, the Department replied that goods were not retained but could be exported in the extended period and that the importer had sought further extension of export period which had been granted upto June 2003 by the Chief Commissioner of Customs (Bangalore). The Department's reply/Chief Commissioner's action is not acceptable since the importer had already achieved the EO by May 2001 and there is no provision in the notification to retain the tools in anticipation of further orders from the supplier.

Reply of the Ministry had not been received (February 2004).

(b) Five consignments of 'squid whole/frozen shrimps' (311220.50 kg) were imported duty free (June to August 1997) by M/s Alsa Marine & Harvest Limited, Chennai, through Custom house (Sea), Chennai for job work and re-export. Of this, the importer re-exported 62000 kg of the finished goods in 1997 and later closed down its unit leaving the balance quantity of 249220.50 kgs unexported on which customs duty of Rs.26 lakh was leviable.

On this being pointed out (February 2002/January 2003), the Department issued (June 2003) an SCN wherein it had been stated that the amount of duty and interest would be recovered from the importers by virtue of the bond and action would be effected after receipt of a reply from the importer to the SCN issued.

Reply of the Ministry had not been received (February 2004).

5.4 Other cases

In 21 other cases, objections were issued to the Ministry on incorrect grant of exemption involving short levy of Rs.92.80 lakh. The Department admitted the objection in six cases

involving Rs.30.74 lakh and reported recovery of Rs.25.42 lakh in four cases as per table below:

(Rupees in lakh)

Sl. No.	Product on which exemption granted	Name of the importers M/s.	Amount short levied	Amount admitted	Amount recovered
1.	Double rail type- trolley	Whirlpool India Limited	9.65	--	--
2.	Olive oil	Nestle India Limited & M/s Ashanath Private Limited	8.32	7.54	7.54
3.	Copper clad laminates	Epitome Components & M/s Akasak Elec.	8.06	--	--
4.	Scientific equipment	National Institute of Ocean Technology	6.74	6.74	6.74
5.	Nickel cathode	Ferro Alloys Corp. & Ambika Steels Limited	6.25	--	--
6.	Hospital beds	PGI of medical services, Rohtak	5.96	Not admitted	--
7.	Amifostine Inj 500	Fulford India Limited	5.44	5.44	6.15
8.	Enamelled copper wire	Hotline Wittis Electronic Limited	5.43	--	--
9.	Knitting machine	Rausheena Exim, Kolkata	5.22	Not admitted	--
10.	Optical fibre cable	AMP India Limited	4.99	4.99	4.99
11.	Parts of CNG kits	Minda Impco Limited	4.24	--	--
12.	Computer cabinet	Supertron Electronics Limited	3.99	3.00	--
13.	Toner cartridges	Gestetner (India) Limited & Cannon (India) Limited	3.43	Not admitted	--
14.	CPU	Vintron Informatics Limited	3.13	Not admitted	--
15	Nylon 6 resin	Superfil Products Limited	3.03	3.03	--
16	Crazy 65 rucksack	Shradha Trading (India)	2.29	Not admitted	--
17	Satellite communication apparatus	Essel Shyam Technologies Limited	1.98	Not admitted	--
18	Hospital furniture	DGAFMS, New Delhi	1.25	Not admitted	--
19	Gonis lens	Multi Instruments, New Delhi	1.21	Not admitted	--
20	Industrial blower	Caryaire Equipments(I) Limited	1.18	Not admitted	--
21	Computer keyboard	NTPC	1.01	Not admitted	--
	Total		92.80	30.74	25.42

CHAPTER VI: SHORT LEVY DUE TO UNDERVALUATION

6.1 Incorrect fixation of Tariff value

According to sub section 2 of section 14 of Customs Act 1962, if the Central Government is satisfied that it is necessary or expedient to do so, it may by notification in the official Gazette, fix the tariff value of any class of import or export goods having regard to the trend of value of such or like goods, and where such tariff values are fixed, the duty shall be chargeable w.r.t. such tariff value. Invoking the provisions of the above section, the tariff value for crude palmolein was fixed at $334 per MT from 7 December 2001 to 15 May 2002 and US$367 per MT from 16 May 2002 onwards.

Audit scrutiny revealed that for 19 consignments of 'crude palmolein' imported by M/s. Ruchi Soya Industries Limited and four others during April to June 2002 through Custom house (Sea), Chennai, the invoice value per MT was higher than the tariff value on which the goods were assessed. The fixation of tariff value lower than the prevalent market value resulted in under valuation of the consignments and consequential loss of revenue of Rs.1.81 crore.

On this being pointed out (October/December 2002), the Department stated (December 2002) that the goods were assessed to duty correctly with reference to the tariff value fixed by the Government of India. There is a need to amend the provisions of sub section 2 of section 14 of Customs Act, 1962 to provide for assessment at the tariff value or invoice value whichever is higher to tighten tax administration and protect revenue.

Reply of the Ministry had not been received (February 2004).

6.2 Incorrect adoption of assessable value

6.2.1 According to section 14 of the Customs Act, 1962, duty of customs is chargeable on any goods by reference to their value. The value of such goods shall be deemed to be the price at which such or like goods are ordinarily sold, or offered for sale, for delivery at the time and place of importation or exportation in the course of international trade where price is the sole consideration for the sale or offer for sale. Rule 10A of Customs Valuation Rules, 1988 prescribes that when the proper officer has reason to doubt the truth or accuracy of the value declared in relation to any imported goods, he may ask the importer of such goods to furnish further information including documents or other evidence and if, after receiving such further information, the proper officer still has reasonable doubt about the truth or accuracy of the value so declared, it shall be deemed that the value of such imported goods cannot be determined under the provisions of sub rule (1) of rule 4 of Valuation Rules.

Audit scrutiny revealed that in five consignments of various chemicals (epichlorihydrin, monosodium glutamate, mannitol, boric acid and calcium carbonate) imported by M/s. Aarti Drugs Limited and four others during January to December 2001 through Nhava Sheva and Mumbai (Sea) Commissionerates, the invoice value was only 13 to 49 per cent of the price indicated in the Chemical Market Reporter (CMR) for the corresponding period. As such the

proper officer should have called for further information under rule 10A of the Customs Valuation Rules, 1988. Failure to do so resulted in short levy of duty of Rs.35.91 lakh.

On this being pointed out (September/December 2001/April 2002), the Department stated (May to July 2002) that the prices indicated in the Valuation Bulletin are not transaction value, they are intended as a bench mark for CMR readers and are not to be used as basis for negotiations between buyers and suppliers. It was also stated that these prices did not necessarily represent the levels at which transactions might have actually occurred nor did they represent bid or asked prices.

Reply of the Department is not tenable for the reason that CMR reports average prices at which transactions take place at a given point of time. Discount of 87 to 51 per cent appears unrealistic. Further, the valuation rules cast a responsibility on the importer to satisfy the authorities that the declared transaction price entered into was in the normal course of international trade and was not hit by any one of the conditions as set out under sub rule (2) of rule 4.

Reply of the Ministry had not been received (February 2004).

6.2.2 In accordance with rule 4 (2) of Customs Valuation Rules 1988 the transaction value of imported goods under rule 4 (1) shall be accepted provided that the sale does not involve any abnormal discount or reduction from the ordinary competitive price.

M/s. Mcdowell and Company Limited, Visakhapatnam imported 1573.044 MT of 'styrene monomer' at the rate of $ 1360 per MT on 12 June 1995 and 3 July 1995, and 734.087 MT at the rate of $ 1390 per MT on 19 June 1995 through New Custom house, Panambur, Mangalore.

Audit scrutiny revealed that for these consignments, two separate purchase orders were placed on the same day (7 April 1995) to the same firm and goods were to be supplied with similar specification. However the rate at which the goods were imported ($1360 and $ 1390 per MT respectively) differed, resulting in short levy of duty of Rs.4.81 lakh.

On this being pointed out in January 2002, the Department while accepting the facts stated that the SCN was not issued as demand was hit by limitation of time, but the matter was being pursued with the firm for recovery of short levy of duty. Further progress was awaited (February 2004).

Reply of the Ministry had not been received (February 2004).

CHAPTER VII: NON LEVY/SHORT LEVY OF ADDITIONAL DUTY

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

Short levy of additional duties amounting to Rs.7.94 crore were reported to the Ministry in 12 cases, as narrated below:

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

7.1.1 It was judicially held (January 2002) by CEGAT in the case of M/s. IOCL vs Commissioner of Central Excise, Vadodara {(2002 (147) ELT-357 (Tri-Del)} that the benefit of concessional rate of additional duty under notification No.3/2001-CE dated 1 March 2001 is not applicable to 'superior kerosene oil' (SKO) cleared for industrial use.

Sixty three consignments of SKO imported (November 2001 to February 2002) for industrial use by M/s. Southern Petro Oils Limited, Chennai and others were assessed at concessional rate of additional duty under the notification ibid. This resulted in short levy of additional duty of Rs.4.27 crore. No action was begun to demand the balance amount of additional duty in the case of clearances made before January 2002.

On this being pointed out (March 2003), the Department stated (May 2003) that demand notices had been issued to the importers. Further progress was awaited (February 2004).

7.1.2 'Sewing machines' other than those with in built motors are exempt from central excise duty vide Central Excise notification Nos.5/99 dated 28 February 1999, 6/2000 dated 1 March 2000 and 3/2001 dated 1 March 2001.

Twenty seven consignments of 'industrial sewing machines' imported by M/s. India Agencies Limited and M/s. Silver Crest Clothing (P) Limited, Bangalore between December 1999 and November 2001 through Air Cargo Complex and ICD, Bangalore were assessed extending the benefit of Central Excise notification Nos.5/99, 6/2000 and 3/2001.

Since the imported machines had in built motors, which were packed separately only for transportation convenience, the goods were not eligible for the exemption ibid. The incorrect application of the notifications resulted in non levy of additional duty of Rs.2.28 crore.

On this being pointed out (April 2000 and January 2002), the Department stated (May 2000 to February 2002) that the sewing machines did not have in built motors but external motors run through a pulley and belt system. Further, it had also been decided in the Commissioner's conference held in Bangalore in June 2000 to extend the benefit of the notifications in cases where the motor was connected externally.

The reply is not tenable as motors were not presented for assessment separately and the invoice entry indicated 'sewing machines as machine complete set'. Hand operation of the

sewing machine was also not possible, and therefore the machines imported were to be considered as having in built motors.

7.1.3 According to Central Excise notification No.6/2002 (serial No.156) dated 1 March 2002 'blankets of wool/yarn' classifiable under Central Excise Tariff heading (CETH) 63.01/55.09/55.10 are exempted from levy of additional duty.

Eighty consignments of old used/premutilated and fumigated synthetic/hosiery/ woollen/acrylic rags imported by M/s S.S. International and others through ICD, Tughlakabad were classified under CETH 63.09/63.10 and cleared without levy of additional duty extending the benefit of notification dated 1 March 2002 even though the goods imported were rags and not blankets. This resulted in short levy of additional duty of Rs.66.37 lakh.

On this being pointed out (October 2002/February 2003), the Department while accepting the facts (March 2003) that rags were not an item of chapter 63 of Central Excise Tariff, stated that benefit of notification No.6/2002 (Serial No.156) had been permitted to facilitate processing of the documents in the FDI system. The Department further stated that goods such as rags falling under heading 63.09/63.10 are not subjected to levy of additional duty.

The reply of the Department is not tenable as it contains a contradiction. On the one hand they had classified rags under chapter 63, and on other hand they stated that it was not an item of chapter 63. The exemption was for blankets classified under 63.01/55.09/55.10 and not for items under heading 63.09/63.10.

Reply of the Ministry had not been received (February 2004).

7.2 Non levy of additional duty due to misclassification

According to notification No.21/2002-Cus dated 1 March 2002 (serial No.80) formulation or bulk drugs classified under chapter 30 of the Custom Tariff specified in the list 3 annexed thereto when imported are exempted from levy of additional duty. Medicaments merit classification under CTH 3004.90/CETH 30.03 and are not covered under the notification ibid.

Five consignments of 'viraferon' and four consignments of 'streptokinase' imported through Air Customs, Mumbai between March to November 2002 by M/s Fulford India Limited and M/s. V.H. Bhagat & Company, Mumbai were classified and assessed under CTH 3002.90/CETH 30.02 without levying additional duty under notification ibid, even though the goods imported were medicaments falling under heading 3004.90 of the Custom Tariff. The misclassification and incorrect exemption resulted in non levy of additional duty of Rs.46.21 lakh.

On this being pointed out (September 2002 to February 2003), the Department reported (February to May 2003) recovery of Rs.30.07 lakh for four consignments. Reply for other consignments was awaited (February 2004).

Reply of the Ministry had not been received (February 2004).

7.3 Short levy of additional duty due to incorrect computation of assessable value

Section 3 (5) of the Custom Tariff Act, 1975 provides for levy of 'Additional duty' in addition to any other duty imposed under the Customs Act, 1962 or under any other law for the time being in force. According to the Medicinal and Toilet Preparations (Excise Duties) Act, 1955, toilet preparations containing alcohol attract excise duty (and also additional duty by aforesaid sub-section (5) of section 3 of the Tariff Act) at 50 percent ad valorem. Further, in terms of section 3 (2) of the said Tariff Act, the value for the purpose of levy of such additional duty shall be the aggregate of the value under section 14 of the Customs Act, 1962 (assessable value) and the basic customs duty under section 12 of the Act including other duties of customs chargeable under any law.

Nine consignments of toilet preparations containing alcohol imported by M/s. Beauty Concept Private Limited and others through Custom house, Kolkata, between May 2001 and May 2002 were assessed to additional duty under the Medicinal and Toilet Preparations (Excise Duties) Act, 1995 based on the assessable value of goods and not on the value according to section 3 (2) of the Custom Tariff Act, 1975. Incorrect determination of value resulted in short levy of additional duty of Rs.9.95 lakh.

On this being pointed out (April to September 2002), the Department while admitting the facts for three consignments involving short levy of Rs.4.74 lakh, reported (December 2002) recovery of Rs.1.03 lakh in August 2002. Reply for the remaining six cases was awaited (February 2004).

7.4 Other cases

In four other cases, incorrect application of rate, incorrect classification, incorrect computation resulted in short levy of additional duty of Rs.16.24 lakh of which two cases involving Rs.9.48 lakh were admitted and recovery of Rs.7.70 lakh reported in one case by the Department, as detailed below:

(Rupees in lakh)

Sl. No.	Details of product	Irregularity	Amount short levied	Amount admitted	Amount recovered
1.	Printed stationery-baggage tags	Non levy of additional duty	6.60	6.60	7.70 including interest
2.	Halogen lamps etc.	Incorrect application of rate	4.79	Not admitted	--
3.	Chewing gum ingredients	Misclassification	2.88	2.88	--
4.	Music-man radio, palito radio	Incorrect computation	1.97	--	--
	Total		16.24	9.48	7.70

CHAPTER VIII: NON LEVY OF SPECIAL ADDITIONAL DUTY OF CUSTOMS

8.1 No mechanism to ensure fulfilment of end use condition

According to notification Nos.17/2001-Cus (serial No.98 and 104) dated 1 March 2001, 3/2001-CE (serial No.58) dated 1 March 2001 and 19/2001-Cus dated 1 March 2001, imports of 'muriate of potash and di-ammonium phosphate' for use as manure or for production of complex fertilisers were subjected to levy of basic customs duty at concessional rate and exempted from levy of additional duty and special additional duty (SAD).

Audit scrutiny of records of Superintendent of Customs, Custom house, Bhavnagar (May 2002) revealed that bulk imports of 55644 MT of 'muriate of potash' and 'di-ammonium phosphate' in August and September 2001 for the purpose of manure by M/s. Indian Potash Limited, Chennai and Indian Farmers Co-operative Limited were provisionally assessed at concessional rate of basic customs duty and exempted from levy of additional duty and SAD. The amount of duty foregone in these cases worked out to Rs.16.55 crore. The assessments were finalised in March/April 2002 and exemption/concessional rate of duty provisionally allowed were treated as admissible though the importers had not furnished evidence that the imported goods were used for the purpose of manure.

On this being pointed out (April 2002 and January 2003), the Department stated (February 2003) that the imports by M/s Indian Potash Limited, a Government of India undertaking are for use as manure or for the production of complex fertilisers and there is no condition to obtain end use certificate in the notification. The Department further stated that the importer had furnished a certificate, at the time of importation, that they had imported cargo for use as manure or for production of complex fertiliser only, and besides had furnished some relevant documents to prove that the fertilisers had indeed been supplied to the farmers for use as manure. However, the Department issued (September 2002) a consolidated demand cum show cause notice for short recovery of Rs.16.55 crore.

The reply of the Department is not tenable in view of the judicial pronouncement by Supreme Court in the case of Collector of Customs, Mumbai vs M/s. Pecific Exports {1998 (99) ELT 488 (SC)} which stated that an importer who is only a trader should adduce evidence to show that the goods imported at concessional rate for specific purpose by him were meant for the stipulated use. Thus, non provision of specific checks and balance as regards actual usage of the goods for intended purposes resulted in not only short levy of duty of Rs.16.55 crore but also in lack of evidence to prove that the largesse had actually been received by the beneficiaries.

Reply of the Ministry had not been received (February 2004).

8.2 Misuse of exemption orders

8.2.1 Imports for sale as such

According to serial No.12 of the notification No.34/98-Cus dated 13 June 1998, goods imported for 'sale as such', other than by way of high seas sales were exempt from payment of SAD provided that the exemption contained therein was not applicable if the importer sold the said imported goods from a place located in an area where no tax was chargeable on sale or purchase of goods. It is clear from the above that the imported goods on subsequent sale which do not suffer the burden of sales tax, cannot enjoy exemption from SAD.

Two importers (M/s. Essel Mining & Industries Limited and M/s. Ruchi Soya Industries Limited, Kolkata) were allowed to import 93,828 MT of 'RBD palmolein' between 13 June 1998 and 28 February 2000 through Custom house, Kolkata (Sea) without payment of SAD amounting to Rs.10.24 crore for subsequent sale under notification ibid. Out of 93,828 MT, 10,736 MT had been sold to 'vanaspati manufacturers' without charging sales tax by virtue of special exemption order issued by the State Government. The sales/purchase, effected within the jurisdiction of the State or made by the vanaspati-manufacturer, do not attract any sales or purchase tax, as the case may be. Thus, both the importers had violated the provisions of the above mentioned notification while selling the imported goods without charging sales tax and so were liable to pay SAD to the extent of Rs.1.42 crore.

The matter was brought to the notice of the Department in February 2001. Their reply was awaited (February 2004).

However, verification of departmental records revealed that the Customs authority had issued two show cause cum demand notices to the importers in November 2001 for recovery of Rs.1.42 crore (Rs.29.79 lakh from M/s. Ruchi Soya Industries Limited and Rs.1.12 crore from M/s. Essel Mining & Industries Limited), the outcome of the adjudication was awaited. Further, the correctness of the audit findings has been confirmed with the judicial pronouncement made by CEGAT, New Delhi in the case of Raj Traders vs Commissioner of Customs, Amritsar {2002 (144) ELT 130 (Tri-Del)}.

Reply of the Ministry had not been received (February 2004).

8.2.2 Imports for trading purpose

According to Customs notification No.29/98 dated 2 June 1998, as amended by notification No.34/98 dated 13 June 1998, special additional duty was exempted for goods imported for trading purpose.

Six consignments of 'ethoxy methylene diethyl ester' imported by M/s. Unimark Remedies Limited, Vapi through Mumbai Commissionerate during June/July 1998 were exempted from levy of SAD under notification ibid on the importer's declaration that these goods were imported for trading. Audit scrutiny, however, revealed that the importer utilised the imported goods for manufacture of finished products and availed Modvat credit towards payment of additional duty (CVD). The imported goods were therefore, not meant for trading purpose. SAD of Rs.8.89 lakh exempted in these cases was therefore, recoverable.

On this being pointed out (September 1998), the Department reported (December 2002) recovery of Rs.8.89 lakh.

Reply of the Ministry had not been received (February 2004).

8.3 Other cases

In three other cases, objections were issued to the Ministry on incorrect grant of SAD involving short levy of Rs.11.43 lakh. The Department admitted the objection in one case and reported recovery of Rs.4.87 lakh as per table below:

(Rupees in lakh)

Sl. No.	Product on which exemption granted	Name of the importers M/s.	Amount short levied	Amount admitted	Amount recovered
1.	Rock phosphate	Sterlite Industries (I) Limited, Tuticorin	4.87	4.87	4.87
2.	Various goods	Kanika Sales & six others	4.53	--	--
3.	Brass scrap and citric acid	Pankaj Metals (P) Limited & Enfield Industries Limited	2.03	--	--
	Total		**11.43**	**4.87**	**4.87**

CHAPTER IX: DUTY EXEMPTION SCHEME

9.1 DEPB Scheme

9.1.1 Credits granted before realisation of export proceeds

According to para 7.25 of the Exim Policy 1997-2002 read with paras 7.38 (ii) and (iii) of HBP Vol. I (1997-2002), if the export proceeds were not realised within six months or such extended period as may be allowed by RBI, the DEPB holder was liable to pay in cash an amount equivalent to the DEPB credit utilised against imports with 24 per cent interest from the date of import till the date of deposit.

Scrutiny of records of the Joint Director General of Foreign Trade (Jt.DGFT), Hyderabad and Kanpur revealed that for 253 post-export licences issued between September 2000 and March 2003, involving export proceeds of Rs.332.51 crore, there was no evidence of receipt of realisation even after six months of exports. In the absence of realisation particulars, DEPB licence holders were liable to pay cash equivalent to DEPB credit of Rs.50.42 crore plus interest.

On this being pointed out (during November 2001 to August 2003), Ministry of Commerce stated (September 2003) that in 170 cases exporters had submitted proof of realisation of export proceeds and that for the balance cases action had been started. Further progress was awaited (February 2004).

9.1.2 Non imposition of restriction on DEPB clearance

According to para 4.46 of HBP Vol. I (2002-07), the CIF value of imports effected under DEPB scheme shall not exceed the FOB value against which the DEPB certificate has been issued.

Ministry of Commerce vide Circular No.26 (RE-99)/99-2000 dated 9 August 1999 clarified that in cases where the clearance of an imported consignment was sought after clubbing different DEPBs, the FOB value taken for CIF restriction should be proportionate to the credit availed against such DEPBs by the importer.

Ninety five consignments of wooden log, coking coal, lam coke and MS scraps imported by M/s. Zenith Timber Products (P) Limited and 22 others during April to December 2002 through Kolkata (Sea) Customs were allowed DEPB benefit under notification No.34/97-Cus dated 7 April 1997 without applying any restriction on CIF value of import against FOB value of DEPB certificate either in single use or in case of their clubbing in single consignments as stipulated in order of 9 August 1999. The omission resulted in undue financial benefit to the importers amounting to Rs.5.11 crore.

This was pointed out to the Department during January to March 2003; reply was awaited (February 2004).

9.1.3 Credit unrelated to actual incidence of duty

DEPB credit at the rate of 5 per cent upto 31 March 2001 and 4 per cent afterwards was admissible on exports of fish and fish products.

M/s. Dhananjaya Impex (P) Limited, Hyderabad and three others were allowed DEPB credit of Rs.1.19.crore during the period July 2000 to January 2002 for export of processed and preserved frozen fish and crustaceans, molluscs and other aquatic invertebrates (cultured black tiger shrimps) weighing 656.230 MTs. The DEPB rate being 5 per cent/4 per cent, credit allowed per kilogram worked out to Rs.18.13 per kg. However, according to standard input output norms (SION), the cost of imported preservatives and packing materials used for export of the aforesaid products worked out to Rs.8.50 per kg. Even if the entire cost of preservatives and packing material is construed as imported and full amount taken as incidence of import duty, the exporters derived extra benefit of Rs.9.63 per kg (Rs.18.13 - Rs.8.50) by way of DEPB credit, which worked out to Rs.63.19 lakh to four exporters.

On this being pointed out (November 2002), Ministry stated (September 2003) that the issue involved a policy matter and DEPB credit was allowed according to DEPB rate list and existing policy provisions.

The fact remains that incorrect fixation of DEPB rate on the basis of deemed import content rather than actual incidence based on industry norms resulted in unintended excess allowance of credit for exports which had relatively little actual import content defeating the spirit of the policy provisions.

9.1.4 Excess grant of DEPB credit due to misclassification

DGFT policy circular No.19 (RE-2000/2001) dated 28 July 2000 clarifies that DEPB credit for export of galvanised iron coils/galvanised steel coils/cold rolled galvanised colour/plain sheets shall be granted according to entry at serial No.363 as distinct from serial No.91 which covers only those goods which are both galvanised and colour coated. The circular also directed that wherever exports of MS galvanised sheets/strips had been granted DEPB benefit under serial No.91, remedial action should be started.

Sixteen consignments of 'galvanised iron coils/galvanised steel coils/cold rolled galvanised colour/plain sheets/cold rolled steel strips' valued at Rs.3.13 crore exported during the year 1997-98 by M/s. Lloyds Steel Industries Limited and M/s. Tata SSL Limited, Mumbai were granted DEPB credit against entry at serial No.91 and allowed credit at the rate 18 per cent, instead of against serial No.363 with credit rate of 4 per cent even though the exported goods were not colour coated. This resulted in excess DEPB credit to the extent of Rs.45.96 lakh.

On this being pointed out (October 2001/June and October 2002), Department issued demands to one exporter. However the Ministry stated (September 2003) that in view of the amendment vide policy circular No.6 (RE-2003) dated 13 June 2003, circular No.19 ibid was made effective from the date of issue i.e. 28 July 2000 and no recoveries were required to be effected.

The fact remains that the delay in implementation of remedial action in cases of exports made prior to July 2000 amounted to excess grant of DEPB credit to the exporter to the tune of Rs.45.96 lakh.

9.1.5 Dual benefit of CENVAT and DEPB

The credit under DEPB scheme is meant to neutralise incidence of customs duty of imports necessary for the manufacture of the final product. In case indigenous raw materials are used for the manufacture of the export goods, they are treated as 'deemed import' and credits are granted. According to Modvat/cenvat rules, credits of specified duties of excise and additional customs duties paid are also available to the exporter.

According to CBEC circular No.68/97-Cus dated 2 December 1997, exporters who avail DEPB credits are not allowed to claim All Industry Rate of Drawback.

It was noticed that M/s. Terumo Penpol Limited, manufacturer and exporter of plastic bags for preserving blood and its components under central excise commissionerate, Trivandrum availed cenvat credit of Rs.19.68 lakh and Rs.1.21 crore and also earned DEPB credit of Rs.13.43 lakh and Rs.19.76 lakh during 1998-99 and 1999-2000 respectively on the indigenous inputs purchased for the manufacture of final products for export under DEPB.

On the analogy of circular No.39/2001-Cus dated 6 July 2001 wherein double benefit of DEPB credit and cenvat/modvat credit was disallowed where brand rate of drawback was claimed, the Government could have imposed restriction on availment of DEPB credit and cenvat credit simultaneously in cases where drawback at All Industry Rate was disallowed. In the absence of any such provision, the exporter availed dual benefit of cenvat and DEPB credits in the instant case.

On this being pointed out (November 2000), Ministry of Commerce stated (September 2003) that the matter involving policy would be examined for corrective measures. Further, Ministry of Finance reported (November 2003) that the subject matter was sub-judice before the High Courts of Mumbai, Delhi and Chennai and that legal recourse for disposal of writ petition in Supreme Court was being contemplated.

9.1.6 Irregular grant of DEPB credit

According to para 4.9 of the Exim Policy 1997-2002, no export shall be made by any person without an importer exporter code (IEC) number unless specifically exempt.

Scrutiny of records of DGFT, Ludhiana revealed that M/s. Metro International, Ludhiana and M/s. Glaze Garments (P) Limited, Ludhiana were allotted IEC numbers 309101136 and 3097011404 respectively. However, DEPB credits were allowed for 20 shipping bills (SB) wherein either IEC numbers mentioned in the SBs did not belong to these firms or no IEC number was mentioned in the SBs. In such absence, credit of Rs.27.11 lakh allowed to these firms was irregular.

On this being pointed out (June 2002), Ministry of Commerce stated (September 2003) that 13 SBs were got corrected and in the remaining, corrective action had been started. Further progress was awaited (February 2004).

9.1.7 Incorrect reckoning of FOB value

According to para 7.38 of HBP Vol. I (1997-2002), effective from 29 September 2000, FOB value for the purpose of granting DEPB credit shall be reckoned only with reference to the buying/selling rate prevalent on the date of negotiation/purchase of shipping bill.

In 67 cases, DEPB credits were sanctioned by the licensing authorities at Coimbatore and Madurai on the basis of FOB value of exports determined with reference to telegraphic/transfer (T/T) buying/selling rate prevalent on the date of realisation of bills instead of the date on which the shipping bills were negotiated/purchased. This resulted in excess DEPB credit of Rs.26.99 lakh.

On this being pointed out (December 2001 and February 2002), Ministry of Commerce stated (September 2003) that of 67 cases, excess credit had been recovered/adjusted in 55 and in two cases, firms had been advised to refund the excess amount paid. In the remaining cases credits were correctly paid.

9.2 EOU scheme

9.2.1 Non fulfilment of EO/NFEP

According to para 98 of Exim Policy read with para 178 of HBP, Vol. I, (1992-97), an EOU is to execute an LUT with the Development Commissioner concerned in the prescribed form given in Appendix XXXI. Vide paras 4 and 7 of the LUT, in case of failure to fulfill the stipulated EO, the unit is liable to pay,

i) the amount of customs duty that would be leviable at the relevant time on the items of plant, machinery, equipment, raw materials, components and consumables, imported duty free by the unit,

ii) excise duty leviable on indigenous goods purchased duty free by the unit,

iii) interest on the duty of customs and excise duties foregone from the date of import/supply to the date of payment of duty,

iv) the liquidated damages as determined by the Development Commissioners.

(a) M/s Zenwell Controls Limited formerly known as M/s. Elcot Power Controls Limited (PCBA Division), an EOU located in MEPZ, Chennai was granted permission (November 1995) for manufacture and export of PCB assemblies valued at Rs.24.65 crore during the period 1996-97 to 2000-01. The value of exports realised was only Rs.14.16 crore amounting to a shortfall of 42.55 per cent in EO. Further the NFEP achieved by the unit was (-) 53.81 per cent for the specified period. As such, it was liable to pay penalty and duty along with interest from the date of import of goods.

Development Commissioner adjudicated (December 2001), the case and imposed penalty of Rs.1 lakh. However, the adjudication order was silent regarding recovery of customs duty of Rs.11.94 crore and interest of Rs.14.22 crore thereon, although Appendix XXXI specifically provided for their recovery. The fact remains that MEPZ authorities failed to recover duty and interest.

On this being pointed out (June 2003), the Customs department/Ministry of Commerce stated (June/December 2003) that there was no relevant authority under which it was empowered to collect duty and interest. The reply is not tenable as exemption notification applicable for the units in EPZs including MEPZ specifically provided for execution of bond with customs authorities to safeguard revenue in case of non fulfilment of EO or non-achievement of the NFEP prescribed. The Ministry of Commerce further stated that the company had registered with the Board of Industrial and Financial Reconstruction (BIFR) as a sick company, as such all other legal proceedings were to be deferred pending the outcome. Further progress was awaited (February 2004).

(b) Scrutiny of records of Bhubaneswar-I Commissionerate revealed that M/s. Ferro Alloys Corporation Limited, Bhadrak, an EOU engaged in the manufacture of 'charge chrome' was granted extension of bonding period for 5 years from 1 April 1999 to 31 March 2004 by the Development Commissioner, Kolkata with the condition to achieve export turnover of Rs.519 crore at the rate of Rs.103.80 crore per annum and NFEP of 60.98 per cent. The unit exported goods worth Rs.139.92 crore upto October 2001 and was closed down in November 2001. As it failed to fulfil the prescribed EO, it was liable to pay customs duty of Rs.11.67 crore and central excise duty of Rs.4.20 crore alongwith interest of Rs.5.36 crore and Rs.1.74 crore respectively on goods imported and procured indigenously. Despite having information about closure of the unit as early as in November 2001, the Department failed to start penal/recovery action according to the LUT.

On this being pointed out (April 2002), the Ministry stated (February 2004) that the unit had deposited Rs.3.94 crore towards customs duty and Rs.0.25 crore towards central excise duty and was finally debonded with effect from 5 September 2003.

Thus, customs duty of Rs.7.73 crore and central excise duty of Rs.3.95 crore besides interest remained unrealised.

(c) According to Customs notification Nos.133/94 dated 22 June 1994 and 53/97 dated 3 June 1997, goods imported for production/manufacture of export articles by an EOU are exempted from customs duty subject to achievement of minimum NFEP and EO as specified in Appendix I of the EXIM Policy. In case of failure, the unit is liable to pay customs duty saved and interest thereon from the date of duty free importation till the payment of such duty.

M/s. S.M. Scrap Recycling (P) Limited, Coimbatore was permitted in January 1994 to manufacture and export ferrous and non ferrous scrap. Against import of goods worth Rs.2.99 crore (including outflow on foreign tour) the unit exported goods valued at Rs.2.94 crore (excluding unrealised export proceeds amounting to Rs.81.38 lakh) upto 1999-2000 against prescribed EO of Rs.3.82 crore and thus achieved NFEP of (-) 1.86 per cent against

prescribed industry norm of 20 per cent. As such the unit was liable to pay duty foregone amounting to Rs.1.84 crore and interest of Rs.1.63 crore. The Development Commissioner, MEPZ in its order in original dated 22 October 2001 condoned the shortfall after taking into account unrealised export proceeds for calculation of minimum NFEP, which was irregular.

This was pointed out to the Department in (March/May 2003); reply was awaited (February 2004).

(d) M/s Sun Granite Exports Limited, Khurda, Bhubaneswar, an EOU was permitted (June 1993) to manufacture and export polished granite slabs worth Rs.34.17 crore with VA of 63 per cent. The unit imported goods worth Rs.6.95 crore under Custom notification Nos.13/81 dated 9 February 1981 and 53/97 dated 3 June 1997 and started commercial production in April 1996. It exported goods valued at Rs.14.77 crore between 1996-1997 and 2000-2001 against the prescribed EO of Rs.34.17 crore, having failed to achieve the prescribed VA. It was therefore liable to pay duty foregone amounting to Rs.1.53 crore and interest of Rs.77.60 lakh.

On this being pointed out (July 2002), the Department stated (January 2003) that SCN for recovery of Rs.1.88 crore towards customs duty foregone on imported goods and Rs.6.67 lakh towards central excise duty foregone on indigenous goods was being started. However the Ministry in their reply (September 2003) reversing the Department stand stated that no provision existed under custom notification No. 13/81 ibid, to demand and recover duty in case of non fulfilment of EO and NFEP for imports made before 3 June 1997. It further stated that though the exporter failed to fulfil EO, it had achieved the minimum NFEP and duty could not be demanded for imports made after 3 June 1997 as the EOU had not violated condition No. 6(iv) of the notification No. 53/97 ibid.

The reply of the Ministry is not tenable as the Ministry vide circular No. 307/5/97-FTT dated 6 August 1997 had accepted the audit contention that customs duty could be demanded and recovered from EOU on imports made under notification No.13/81 ibid (ie before June 1997) in case of their failure to achieve stipulated VA/EO. Further, as regards recovery of duty on imports made under customs notification No.53/97 ibid, the EOU was bound to discharge EO specified in letter of intent/letter of permission (LOI/LOP) as stipulated in para 98 of the Exim Policy 1992-97. Para 179 of HBP, Vol I (1992-97), provides that VA specified in the Exim Policy indicates only minimum level, the Board of Approval being competent to prescribe higher percentages, where warranted, as in the instant case. Further progress was awaited (February 2004).

(e) M/s. Korin Plastics Private Limited, Chennai, an EOU was permitted (November 1996) to manufacture recycled pet flakes. The unit executed an LUT with MEPZ authorities in January 1997. The minimum EO required to be achieved during the years 1998-99 and 1999-2000 was Rs.2.01 crore. However, the unit exported goods worth only Rs.6.86 lakh during these years, the shortfall in EO being 96.59 per cent. Further, the unit achieved NFEP of (-) 117.6 per cent against prescribed minimum of 20 per cent. Failure to achieve the EO/NFEP, invited liability to pay duty and interest (upto March 2003) of Rs.68.47 lakh.

The SCN issued (July 2002) by the Development Commissioner was adjudicated upon (December 2002), and a penalty of Rs.5 lakh imposed but the adjudication order could not be delivered as the unit had apparently moved to some other location. The MEPZ authorities failed to invoke the LUT and the Customs authorities had taken over (September 2001) the finished and capital goods for disposal.

On this being pointed out (June 2003), the Ministry stated (December 2003) that the finished goods were sold in public auction for Rs.3 lakh and efforts made to auction the capital goods for recovery of duty and interest were not successful. The fact remains that improper monitoring by the MEPZ/customs authorities led to revenue amounting to Rs.65.47 lakh remaining unrealised.

(f) M/s. AMJ Narrow Fabrics (P) Limited, an EOU under Falta Export Processing Zone (FEPZ), Kolkata was permitted (September 1994) to manufacture and export narrow fabrics-elastic tapes with stipulated VA/NFEP of 37 per cent. The unit was later permitted (May 1999, August 1999 and February 2000) to manufacture and export 'yarn' (cotton, synthetic and blends) and polyester staple fibre under broad banding by the Development Commissioner which it did by purchasing them from sister unit who had only trading activity. Verification revealed that the unit had no infrastructure for manufacture of synthetic yarn, cotton yarn or polyester staple fibre. As such export of these items did not qualify for fulfilment of EO. Only the item 'narrow fabrics-elastic tapes' justified inclusion in the calculation for achievement of VA/NFEP as the unit manufactured the said item by use of imported 'high speed needle loom/weaving loom for narrow fabrics'. For the period 1995-2000, the unit achieved NFEP of 10.42 per cent as against norm of 20 per cent and was liable to pay Rs.26.91 lakh being the amount of duty foregone in addition to interest payable thereon.

On this being pointed out in March 2002, the Ministry of Commerce stated (December 2003) that a provisional demand notice for realisation of duty had been raised against the EOU.

Reply of the Ministry of Finance was awaited (February 2004).

9.2.2 DTA sale

According to para 9.9 (b) of the Exim Policy 1997-2002 read with para 1(f) of Appendix 42 of HBP, Vol. I (1997-2002), advance DTA sale permission for trial production shall not exceed the entitlement accruable on exports envisaged in the first year and such sale shall be adjusted against subsequent entitlements in maximum period of two years. The unit shall execute a bond with the Assistant Commissioner, Customs/Central Excise concerned to cover the difference between the amount of duties paid on advance DTA sale and full duties applicable on such goods.

(a) The Development Commissioner, Visakhapatnam Export Processing Zone, Vizag granted advance DTA sale permission to M/s. Om Shanti Satins Limited and three other EOUs for a total value of Rs.30.75 crore during the period December 1996 to November 2000, against which the units availed DTA sale to the extent of Rs.30.24 crore. Scrutiny revealed that except part adjustment of Rs.6.99 crore in case of M/s. Om Shanti Satins Limited and M/s. SML Dye Tex Limited, the units had failed to adjust advance DTA sale

valued at Rs.23.25 crore. As such they were liable to pay differential duties applicable amounting to Rs.7.81 crore.

On this being pointed out (November 2002), the Department while accepting the facts for three EOUs stated (April/June 2003) that as the fourth unit (M/s. Kumar Cottex Limited) failed to achieve VA/NFEP, the advance DTA sale could not be adjusted. The reply of the Department is not tenable as permission for advance DTA sale is given for entitlements accruable against exports envisaged in the first year and the unit is expected to achieve VA/NFEP within two years of commencement of commercial production. The Department therefore cannot postpone the adjustment of advance DTA sale for an indefinite period of time on this ground as it would enable the unit to take advantage of its own default in not achieving the VA/NFEP. Further progress was awaited (February 2004).

(b) M/s. Arham Spinning Mills Limited, Jalalpur, Patiala, an EOU under the Central Excise Commissionerate, Chandigarh cleared finished goods (including waste) valued at Rs.26.30 crore in DTA on payment of concessional duty against FOB value of Rs.39.92 crore of exports made during the period 2001-02. Against entitlement of Rs.19.96 crore (being 50 per cent of Rs.39.92 crore), the unit effected DTA sales of Rs.26.30 crore resulting in excess DTA sale of Rs.6.34 crore. Differential duty of Rs.1.64 crore on excess DTA sale besides interest of Rs.38.97 lakh was recoverable.

On this being pointed out (May 2002), the Ministry of Commerce stated (December 2003) that clearances were made on permission granted according to the guidelines provided in the HBP which are valid for one year from the date of issue.

The reply of the Ministry is not relevant as audit was not contesting the DTA clearances but only those cleared more than the entitlement of 50 per cent of FOB value of physical exports during the period 2001-02. The audit contention was later substantiated by the Department by issuing an SCN in March 2003. Further progress was awaited (February 2004).

(c) M/s. MB Inno-tech (India) Limited, Kolkata, an EOU in FEPZ was permitted (October 1997) to manufacture and export 'polystyrene cups and containers and packaging materials made out of polystyrene'. During the period 1999-2003 the unit achieved NFEP ranging between (–) 295.37 per cent and (-) 65.92 per cent against the prescribed minimum NFEP of 20 per cent up to 31 March 2001 and 10 per cent afterwards. The unit had effected DTA sales of Rs.2.78 crore up to June 2002 on payment of concessional duty of Rs.85.09 lakh. As the unit had failed to achieve minimum NFEP, the DTA sales were irregular and it was liable to pay differential duty of Rs.86.28 lakh.

On this being pointed out (February 2003), the Ministry of Commerce admitted (December 2003) the facts and reported that the case was under adjudication by the Commissioner of Customs (Airport and Administration).

Further progress was awaited (February 2004).

9.3 Advance licensing scheme

9.3.1 Non fulfilment of EO

(a) Nil exports

According to para 128 of the HBP Vol. I (1992-97) and para 7.28 HBP Vol. I (1997-2002), if the EO is not fulfilled both in terms of quantity and value, the licence holder of the advance licence shall for regularisation, pay:-

i) to the customs authority, customs duty on the unutilised imported material alongwith interest thereon;

ii) to the licensing authority, a sum in rupees which is equivalent to the CIF value of the unutilised imported materials; and a sum in rupees equivalent to the shortfall in EO.

In addition, the licencee was also liable to penalty under section 11 (2) of Foreign Trade (Development & Regulation) Act, 1992.

Two advance licences were issued to M/s Goodluck Exports, Moradabad and M/s. Monk Seal Impex, Ludhiana in February 1996 and August 1998 by respective licensing authorities for duty free import of goods valued at Rs.90.10 lakh with EO of Rs.1.71 crore to be fulfilled within a period of 18 months from the date of issue of the licences. Against import of raw material valued at Rs.96.06 lakh, the licencees failed to export any goods and were therefore liable to pay (i) customs duty of Rs.49.55 lakh on unutilised material alongwith interest of Rs.66.17 lakh (ii) Rs.1.71 crore equivalent to shortfall in EO and Rs.96.06 lakh being value of the unutilised imports. In addition penalty of Rs.4.13 crore under FT (D&R) Act 1992 was also leviable.

On this being pointed out (May/December 2002/January 2003), the Department confirmed penalty of Rs.13 lakh in one case in March 2003. In the other, Ministry of Commerce while accepting the facts stated (September 2003) that adjudication order had been passed against the firm and if no appeal was preferred, the district authority would be requested to recover the penalty as arrears of land revenue. Further progress was awaited (February 2004).

(b) Partial exports

(i) A quantity based advance licence was issued (November 1997) to M/s. Uttam Steel Limited, Mumbai by the licensing authority, Mumbai for duty free import of Rs.6.46 crore against EO of Rs.8.59 crore. The licencee could export goods worth Rs.6.36 crore having imported goods of Rs.5.53 crore. Rs.27.89 lakh towards customs duty on unutilised imports alongwith interest of Rs.33.47 lakh thereon became payable on account of failure to achieve prescribed EO. In addition Rs.80.83 lakh on the sum equivalent to the unutilised imports and Rs.2.23 crore equivalent to the shortfall in the EO were also payable.

This was pointed to the Department (December 2002); reply was awaited (February 2004).

(ii) M/s. BPL Limited, Bangalore was issued an advance licence (October 1998) for duty free import of US$ 72,99,416 against EO of US$ 82,35,000. The validity of the licence was

upto 04 April 2000. The licence was amended (March 2000) on the request of the importer to import components of CIF value US$ 67,63,260 and FOB value of exports of US$ 76,86,000.

Scrutiny revealed that the importer achieved EO of US$ 64,12,464 as against prescribed EO of US$ 76,86,000 resulting in shortfall in EO to the extent of US$ 12,73,536 upto the validity of licence. Consequently he was liable to pay customs duty on unutilised imports alongwith interest of 24 per cent thereon and surrender special import licence (SIL) of a value equivalent to shortfall in EO. The Department however had not started action to recover the duty.

On this being pointed out (August 2001), the Ministry reported (September 2003) recovery of an amount of Rs.33.25 lakh towards customs duty and interest and further stated that the issue of fresh licence and export benefits to importer had been discontinued with effect from 21 March 2003.

9.4 Export promotion capital goods (EPCG) Scheme

Shortfall in EO

9.4.1 Nil export

According to para 38 of the Exim Policy 1992-97 read with para 106 of the HBP Vol. I (1992-97), an EPCG licencee is permitted to import capital goods at concessional rate of customs duty subject to fulfilment of prescribed EO within the stipulated period and in case of failure to do so, he is liable to pay customs duty plus interest thereon.

Eleven EPCG licences were issued between July 1994 and May 1997 to M/s Metazinc (India) Limited, Maharastra and nine others by the licensing authorities at Mumbai, Hyderabad and Bangalore for import of capital goods valuing Rs.9.64 crore at concessional rate of duty against prescribed obligation of Rs.38.46 crore. But the licencees, having imported goods worth Rs.9.64 crore during the EO period failed to export any goods. They were thus liable to pay duty foregone amounting to Rs.2.54 crore plus interest of Rs.3.28 crore (upto March 2003).

On this being pointed out between March 2001 to February 2003, Ministry of Commerce/Finance stated (September 2003/January 2004) that SCNs were issued in four cases, in two cases licencees applied for extension, in one case the licencee fulfilled EO and in one case SCN had been adjudicated imposing a penalty of Rs.1.20 crore. In two other cases the licencees were declared defaulters. Reply for one case was awaited (February 2004).

9.4.2 Partial export

Two EPCG licences were issued (September 1994/December 1996) to M/s. Arviva Industries Limited, Mumbai and M/s. Indore Wire Company by the licensing authority at Mumbai, for import of capital goods valuing Rs.14.67 crore at concessional rate of duty against prescribed EO of Rs.58.06 crore. They exported goods worth Rs.32.50 crore during EO period against import worth Rs.14.27 crore. Proportionate duty saved amounting to Rs.86.78 lakh plus interest of Rs.1.51 crore upto March 2003 was recoverable from the licencees.

On this being pointed out (December 2001/November 2002), the customs department stated (May 2002) that in respect of M/s. Arviva Industries Limited, Mumbai a SCN had been issued.

Ministry of Commerce in their reply stated (September 2003) that the party had filed a writ petition before the Hon'ble High Court, Mumbai against the demand notice issued for the shortfall and forfeiture of the Bank Guarantee (BG). Since the case is sub-judice, action would be taken according to direction of Hon'ble Court.

Reply of the Ministry of Finance had not been received (February 2004).

9.4.3 Inadmissible exports

An EPCG licence was issued (July 1997) to M/s. Seva Medicals Limited, Mumbai for import of capital goods worth Rs.1.73 crore at concessional rate of duty against export of disposable needle for syringes worth Rs.6.92 crore but glass syringes instead of disposable needles were exported. As such the duty foregone amounting to Rs.74.87 lakh plus interest of Rs.66.42 lakh (upto March 2003) was recoverable from the licencee.

On this being pointed out (November 2002), the Department stated (March 2003) that the licencee was declared a defaulter in February 2003. Further progress was awaited (February 2004).

9.5 Other cases

In 21 other cases of non fulfilment of EO/VA, irregular DTA sales, excess DEPB credits etc., short levy of Rs.1.41 crore alongwith interest of Rs.67.95 lakh were pointed out as per table below. Department/Ministry admitted objections in 14 cases.

(Rupees in lakh)

Sl. No.	Irregularity	Name of the importers/ exporters (M/s.)	Commi-ssionerate	Amount objected	Interest	Whether accepted
1.	Imports not specified in SION	Grasim Industries Limited	Bhopal	17.60	--	No
2.	Excess DTA entitlement	Nitin Spinners Limited, Bhilwara	Jaipur	15.23	--	Yes
3.	Non imposition of late cut on application for replenishment licences	Tanvi Exports, Jaipur & four others	New Delhi	10.17	--	Yes
4.	Non realisation of export proceeds	Gandhar Petrochemicals Limited	Mumbai	9.81	6.08	No
5.	Incorrect issue of DEPB certificate	Shimpo Exports & 3 others	Kolkata	9.30	--	Yes
6.	Excess utilisation of imported goods	Ashima Denims, Ahmedabad	Mumbai	9.23	11.44	Yes
7.	Short collection of duty and interest	Super Spinning Mills, Coimbatore	Tuticorin	9.22	--	Yes
8.	Non fulfilment of EO	Srinivasa Fine Arts Limited, Sivakasi	Madurai	8.37	3.60	Yes

9.	Non fulfilment of EO against EPCG licences	Forma Sports (P) Limited, Mumbai	Mumbai	8.23	10.69	Yes
10.	Incorrect grant of exemption under DEPB	Birla Tyres & M/s. SAIL	Kolkata	8.04	--	No
11.	Excess grant of DEPB credit	Dr. Reddy's Labs Limited, Hyderabad & others	Hyderabad	6.55	--	Yes
12.	Improper grant of DEPB credit	RCC Sales (P) Limited, Hyderabad	Hyderabad	6.36	--	No
13.	Non fulfilment of EO	Jai Bharat Overseas Limited, Surat	Surat	2.48	2.81	Yes
14.	Non imposition of late cut on application for Replenishment licence	Growmore Connections Inc., Jaipur & two others	New Delhi	5.02	--	Yes
15.	Non fulfilment of EO against EPCG licence	Boroplast (P) Limited, Mumbai	Mumbai	4.62	7.94	Yes
16.	Irregular DTA sales	Rama Scrap Recycling (P) Limited, Gandhidham	Kandla	4.36	7.79	Yes
17.	Non fulfilment of EO against EPCG licence	Mamata Exports (P) Limited, Bangalore	Bangalore	2.39	4.40	Yes
18.	Excess DEPB credit	Sri Lakshmi Saraswathi Textiles Limited, & others	Chennai	1.84	--	Yes
19.	Excess DEPB credit	Jansons Exports, Thiruchengode	Coimbatore	1.80	--	No
20.	Non fulfilment of EO against EPCG licence	G. Claridge & Company Limited	Mumbai	0.85	1.39	No
21.	Non recovery of interest	Babu Spinning Mills, Madurai & one other	Chennai	--	11.81	Reply awaited
	Total			141.47	67.95	

CHAPTER X: OTHER TOPICS OF INTEREST

10.1 Non-realisation of penalties

10.1.1 According to section 112 of the Customs Act 1962, any person who imports goods which are liable to confiscation under section 111 of the said Act, shall be liable to penalty in the case of goods for which any prohibition is in force under this Act or any law for the time being in force.

Scrutiny of records of three Custom Commissionerates (Patna, Tuticorin and Kanpur) revealed that penalties amounting to Rs.11.02 crore imposed in 1651 cases under section 112 of the Act ibid, remained unrealised as on 31 March 2003.

On this being pointed out (January 2002 to September 2003), the Department/Ministry reported (January/November 2003) recovery of Rs.4.50 lakh in 318 cases, initiation of certificate action in 121 cases, writing off of an amount of Rs.28.75 lakh in 18 cases and considering action of writing off of Rs.83.89 lakh in 277 cases. In 662 cases persuasive action had been initiated. Further progress was awaited (February 2004).

10.1.2 Audit scrutiny of records of ICD, Bangalore revealed that personal penalties and redemption fine amounting to Rs.16 lakh imposed on M/s. Prajwal Exports, Bangalore in May 1999 for clandestine removal of export cargo remained outstanding for realisation.

On this being pointed out (August 2002), the Department reported (August 2003) recovery of Rs.4.52 lakh. Further progress was awaited (February 2004).

10.2 Loss of revenue due to delay in implementation of CEGAT order

According to notification No.22/98-Cus dated 6 May 1998, the anti-dumping duty on 'metallurgical coke' imported from China was chargeable in rupee terms. CEGAT however, in its final order on 21 January 2000 held that the anti dumping duty rate should be a specific rate and fixed in dollar terms varying from $18.35 to 24.95 depending on exporter. Though the decision was accepted, the Customs notification to give effect to it was issued only on 19 May 2000 but without retrospective effect.

Scrutiny revealed that 14 consignments of 'met coke' imported from China between 21 January 2000 and 18 May 2000 through Bhubaneswar and Chennai (Sea) Commissionerates were cleared by charging anti dumping duty in rupee terms and at the rates prevailing before the CEGAT decision. Delay in implementation of CEGAT order ibid resulted in loss of revenue of Rs.6.49 crore.

On this being pointed out (December 2001/June 2003), the Department (Bhubaneswar Commissionerate) stated (September 2002) that they could have levied the anti dumping duty only on the basis of a notification and that they were not responsible for delay in its issue. Reply for import through Chennai (Sea) Commissionerate was awaited (February 2004).

Reply of the Ministry had not been received (February 2004).

10.3 Non-levy of duty on imported aviation turbine fuel (ATF) consumed during converted domestic flights

Section 87 of the Customs Act, 1962 provides that any stores on board a vessel or aircraft imported without payment of duty, be consumed thereon as stores during the period such vessel or aircraft is a foreign going vessel or aircraft. Wherever an international flight is converted into a domestic flight at the end of its foreign run, the provision of section 87 ibid is no longer fulfilled and so the stores on board which are consumed during such converted domestic run attract customs duty.

M/s. Indian Airlines, while commencing international journey from Dum Dum airport, Kolkata lifted ATF without payment of duty from M/s. IOCL, in addition to their duty paid stock lying in the aircraft. Similarly, on its return journey, the Airlines regularly uplifted ATF from Dhaka, Bangkok, Rangoon and Kathmandu. The Airlines after termination of the foreign run at Dum Dum airport converted the flight into domestic flights to Mumbai, Delhi, and Chennai. However, the customs authority at Dum Dum airport did not levy duty on imported ATF left on board at the time of conversion from international flight to domestic flight, and Indian Airlines also did not pay duty thereon. The omission resulted in non levy of duty of Rs.2.97 crore during June 2001 and October 2002.

On this being pointed out (March 2002 and February 2003), the Department intimated (May 2003) that three split up show cause cum demand notices covering the period May to October 2002 were issued in May 2003. The recovery particulars including issue of demands for earlier period (June 2001 to October 2001) have not been received (February 2004).

10.4 Import of spares after initial setting up of a power project

In accordance with the provisions of the Project Import Regulations, 1986 and conditions stipulated in Customs Tariff heading 98.01, all machinery, equipments, spare parts etc. required for the initial setting up of a unit are eligible for concessional assessment. Further, the importer is to, within three months from the date of clearance of the last import, submit a statement indicating the details of goods imported together with necessary documents to finalize the project contract.

Five 'generators' imported by M/s. Kerala State Electricity Board under a power project contract were commissioned in November 1998 with commercial operation commencing in December 1998. Spare parts valued at Rs.4.34 crores were allowed to be imported through Air Customs, Trivandrum at concessional rate during the period March 2000 to September 2002 even after commercial production of the project had begun. Due to inaction on the part of the Department towards finalisation of the project contract even after commencement of commercial operation, imports of spare parts continued to be allowed, which was irregular. This resulted in short levy of Rs.2.47 crore.

On this being pointed out (November 2002/May 2003), the Department while admitting the facts stated (June/July 2003) that such irregular imports were already in the knowledge of the Department (September 2002). They further stated that 17 such imports were denied the benefit of concessional duty and a demand for Rs.2.47 crore had been issued (June 2003). However the fact remains that imports at concessional rates continued even after three years of commissioning indicating that there was no monitoring mechanism to keep such imports in check. Further, the demand was issued as late as in June 2003.

Reply of the Ministry had not been received (February 2004).

10.5 Delay in recovery of confirmed demand

Customs department (Chennai) issued a demand notice under section 72 of the Customs Act, 1962 to M/s. Almetal Recycling Private Limited, Chennai in October 2000 for duty of Rs.45.80 lakh plus interest for not achieving EO/VA against duty free import, which was confirmed in October 2001 by which time validity of the bonds executed by the unit with the Customs department binding itself to fulfilling the EO had expired. The licensing authority imposed a penalty of Rs.0.50 lakh in March 2002, which was recovered in August 2002. However the demand confirmed in October 2001 remained unrealised till date. Inaction on the part of the Department to realise the amount led to blockage of revenue of Rs.45.80 lakh and interest of Rs.59.12 lakh thereon.

This was pointed out to the Department in April 2002; reply was awaited (February 2004).

10.6. Delay in disposal of uncleared goods

According to section 48 of the Customs Act, 1962, if imported goods are not cleared for home consumption or warehoused or transhipped within 30 days from the date of unloading, such goods may, after notice to the importer and with the permission of proper officer be sold by the person having the custody thereof.

One hundred and eleven consignments of various goods valued at Rs.6.12 crore involving duty of Rs.98.32 lakh imported during October 1997 to July 2002 through Custom houses, Tuticorin and Bangalore lying in port area were pending disposal for a period between 7 months to 70 months due to inaction by the custodian/department leading to blockage of revenue amounting to Rs.98.32 lakh.

On this being pointed out (July/December 2002/August 2003), the Customs authorities at Bangalore reported (May 2003) that action had been started under section 48 of the Act to dispose of the goods. Further, the customs authorities at Tuticorin stated (December 2003) that 25 consignments were disposed of fetching Rs.13.69 lakh, nine consignments were got cleared by the importers at a later date and the remaining consignments could not be auctioned after several attempts for want of fair price fixed for them. Further progress was awaited (February 2004).

10.7 Excess payment of drawback

On export of goods, refund of excise and customs duties paid on components and raw material could be claimed as drawback according to provisions in the relevant Acts and rules thereunder. Of 14 cases, where excess payment of drawback amounting to Rs.4.44 crore had been pointed out, the Department/Ministry admitted the facts in 12 cases and reported recovery of Rs.27.20 lakh in eight cases.

10.8 Loss of revenue due to absence of provision in the Act/rule to levy interest

According to rule 16A of the Drawback Rules 1995, where export proceeds have not been realised, the amount of drawback paid has to be recovered. However, there is no provision in the Act/rule for levy of interest on such drawback recovered.

Drawback of Rs.70.74 lakh paid (February 1999 to May 2003) to 57 exporters by Chennai (Sea) and Tuticorin Custom houses, was recovered according to rule 16A as export proceeds were not realised. However, interest on such irregular drawback paid could not be recovered, as there was no provision in the Act/rule to charge it. Absence of provision to levy interest had resulted in loss of revenue of Rs.16.40 lakh.

This was pointed out to the Department in April/June 2003, the Ministry while admitting the facts of absence of provision stated (December 2003) that drawback in such cases was neither irregularly nor erroneously paid and considered provisions of interest too harsh.

However, the fact remains that such provisions exist in other export incentive schemes such as DEPB, DEEC, the absence of which in the Drawback rules led to loss of revenue.

10.9 Non levy of anti-dumping duty

10.9.1 According to notification No.01/2002-Cus dated 2 January 2002, 'lead acid batteries' classified under Customs Tariff heading 85.07 imported into India from Bangladesh attract anti dumping duty.

Eight consignments of 'lead acid batteries' imported by M/s Akuram Enterprise from Bangladesh in January/February 2002 through Commissionerate of Customs (Preventive), West Bengal were assessed/cleared without levying anti dumping duty under notification ibid. This resulted in non levy of duty of Rs.35.44 lakh.

On this being pointed out (March/April 2002), the Department raised demand (June 2002) in six cases involving Rs.23.73 lakh. Further progress was awaited (February 2004).

10.9.2 According to notification No.100/98-Cus dated 27 November 1998, import of 'steel plates' classified under Customs Tariff heading 72.08 from Ukraine attract anti dumping duty at the rate equivalent to the difference between Rs.22000 per metric tonne and the landed value of the goods.

Three consignments of 'non-alloy steel plates' classified under Customs Tariff heading 7208.25 imported by M/s. Shah Brothers and Company in December 2002 from Ukraine through Sea Customs, Mumbai were cleared without levying anti-dumping duty. This resulted in non-levy of duty of Rs.31.64 lakh.

The matter was pointed out to the Department in April 2003; reply was awaited (February 2004).

10.10 Non-recovery of interest on delayed payment of inland air travel tax (IATT) and foreign travel tax (FTT)

Vide public notice No.26/94 dated 1 September 1994 read with public notice No.1/2002-IATT and FTT dated 4 January 2002, each carrier/airline authorised to collect IATT was required to pay into treasury, such tax collected in any month within 30 days from the end of the month failing which the carrier would be liable to pay interest for the entire period for which payment of such tax had been delayed.

Scrutiny of records of Customs Commissionerates, Delhi and Cochin revealed that in 125 cases of M/s. Sahara Airlines and others, interest of Rs.30.34 lakh for the delayed remittance was not recovered. Out of 66 cases in Delhi Commissionerate, SCNs issued during May 2001 to May 2002 for 49 cases were yet to be adjudicated while in the remaining cases no action was started to recover the interest.

On this being pointed out (August 2002 to March 2003), the Cochin Commissionerate reported (April 2003) recovery of Rs.0.07 lakh in one case and the Delhi Commissionerate while accepting the facts in 36 cases stated (July 2003) that adjudication proceedings were under progress. Replies in remaining cases are awaited (February 2004).

10.11 Loss due to shortage of seized goods

According to the CBEC instructions dated 13 June 1961 and 25 July 1968, a complete verification of seized and confiscated goods is required to be conducted every six months. Precious and semiprecious stones were included (December 1997) in the list of valuable seized goods in notification No.31/86-Cus dated 5 February 1986 issued under section 110 (IA) of the Customs Act, 1962 which empowered the Government to dispose of seized goods immediately even before adjudication.

Audit scrutiny of the records of Deputy Commissioner of Customs, Imphal revealed that neither was periodical stock taking done nor was action for early disposal taken as envisaged in the instructions ibid, for 23 consignments of 'precious stones', seized/confiscated between October 1992 and December 1997 (assessed at Rs.30.94 lakh) The inaction/negligence by the customs authorities led to shortage of 13 consignments valued at Rs.19.80 lakh.

On this being pointed out (November 1998), the Department while accepting the facts stated (November 2002) that 13 consignments valued at Rs.19.80 lakh were missing since 1998, six consignments were physically available and four consignments were disposed of.

Reply of the Ministry had not been received (February 2004).

10.12 Non levy of cess

Ten consignments of 'coking coal' and 46 consignments of 'degummed soyabean oil and palm oil' imported during February and December 2002 by M/s. Steel Authority of India Limited, Kolkata and two others through Kolkata and Mumbai Commissionerates were cleared without levying cess of Rs.19.12 lakh.

The matter was pointed out during July 2002 to April 2003. Subsequent verification (May 2003) revealed that the Kolkata Commissionerate had requested the importer to pay the amount voluntarily for eight consignments involving duty effect of Rs.3.87 lakh. However, reply of the Department had not been received (February 2004).

10.13 Excess levy of duty

'Integrated circuits' (ICs) classified under Customs Tariff heading 85.42 were chargeable to 'nil' rate of duty.

Ten consignments of 'ICs' imported by ISRO Satellite Centre, Department of Space, GOI between April 2002 to August 2002 through Air Custom, Bangalore were classified under heading 8542.29 and assessed to concessional rate of duty under the notification No.51/96-Cus dated 23 July 1996 instead of at 'nil' rate. This resulted in excess levy of duty of Rs.31 lakh.

On this being pointed out between September 2002 and November 2002 the Department accepted the excess charge of duty (May 2003).

10.14 Other cases

Of 18 cases, which audit pointed out involving Rs.1.17 crore as detailed below, the Department accepted objections in nine cases involving duty effect of Rs.66.40 lakh and reported recovery of Rs.26.97 lakh in six of them.

(Rupees in lakh)

Sl. No.	Subject	Importer/exporter M/s.	Amount objected	Amount admitted	Amount recovered
1.	Delay in recovery of fees	Ruchi Soya Industries	14.58	14.58	11.74
2.	Duty on ship stores	CC, Visakhapatnam	13.93	13.93	--
3.	Disposal of confiscated goods	Punalur Paper Mills Limited	13.03	--	--
4.	Recovery of confirmed demand	Veerakumar Spinning Mills Limited Tuticorin	11.00	--	--
5.	Non levy of anti dumping duty	Allied Photographics (I) Limited	9.37	9.37	1.66
6.	Incorrect computation of landed value	New Generic Drug house Limited Gujarat.	6.82	--	--
7.	Non levy of anti dumping duty	SAIL	6.31	6.31	--
8.	Non realisation of penalty	Indian Airlines & Singapore Airlines	5.86	5.86	4.08
9.	Non levy of special excise duty	S.V. Silvary Textiles	5.82	5.82	2.51
10.	Incorrect computation of landed value	Turakhia Ferromet Limited	5.39	Not admitted	--
11.	Non levy of anti dumping duty	Harbanslal Malhotra & Sons Limited, & M/s. SAIL	4.44	Not admitted	--
12.	Incorrect duty rates	Kodak India Limited	3.85	3.85	3.85
13.	Incorrect computation of landed value	Shah Fabricators (P) Limited, Thane	3.68	--	--
14.	Excess baggage allowance	ITDC Duty Free Shop, Kolkata	3.55	3.55	--
15.	Non levy of anti dumping duty	MRF Limited, Chennai	3.13	3.13	3.13
16.	Non levy of anti dumping duty	Shital International & Aabhas Spinners (P) Limited	3.10	--	--
17.	Incorrect computation of landed value	Isochem, Mumbai	1.90	--	--
18	Incorrect computation of landed value	Kantilal Manilal & Company Limited, Bhiwandi	1.03	--	--
	Total		116.79	66.40	26.97

10.15 Miscellaneous

341 other cases involving duty of Rs.90.34 lakh were also pointed out. The Department has accepted all the objections and reported recovery of the amount.

Minakshi Ghose

New Delhi
Date: 28 April 2004

(MINAKSHI GHOSE)
Principal Director (Indirect Taxes)

Countersigned

New Delhi
Date: 28 April 2004

(VIJAYENDRA N. KAUL)
Comptroller and Auditor General of India