



CHAPTER

1

GENERAL





1.1 Introduction

The consumption of alcohol is perhaps as old as civilisation itself. Throughout the history of the world, this has been associated with revelry and feasting. India is one of the leading consumers of alcohol in the world. The reality about alcohol consumption is that the developed countries are consuming less and in contrast, consumption in developing countries is increasing (WHO, 2004). The future market for alcohol is in the developing world, particularly in Asia. According to a report published by market research firm International Wine and Spirit Record (IWSR), the total consumption of spirits in the country stood at 200 million cases¹ in 2009 and it was expected to increase by 8 per cent in 2010.

1.2 Legislative provisions

India's Constitution declares that the State shall endeavour to bring about prohibition of the consumption of intoxicating drinks. Conversely, the State Governments, under another constitutional provision, levy Excise Duty on goods like liquors, opium, Indian hemp and other narcotic drugs and countervailing duties on similar goods manufactured elsewhere and brought into the State. Therefore, since independence successive governments have followed different policies on alcohol and the deregulation of this sector is being generally encouraged due to its potential for significant contribution to the exchequer of the State.

1.3 Prohibition

The Directive Principles of State policy spell out the policy of "Prohibition" in the Constitution of India. Article 47 of the Constitution of India says "the State shall regard the raising of the level of nutrition and standard of living of its people as among its primary duties and in particular, the state shall endeavour to bring about prohibition of the use except for medicinal purposes, of intoxicating drinks and of drugs which are injurious to health".

The Andhra Pradesh State had introduced prohibition for the first time in 1948 and it was relaxed subsequently in 1969. It was reintroduced in 1995 and relaxed again in 1997.

1.4 Activities of the Department

The Department deals with regulation, possession, production, manufacture, selling, buying and transport of liquor. Excise Revenue is the second largest source of tax revenue for the State. The Department plays a dual role of enforcing prohibition of arrack and procuring revenue through regulation of Indian Made Foreign Liquor (IMFL) and Toddy. The Department, along with other State and Central Government agencies also enforces the law relating to Narcotics and Psychotropic substances. The Department is responsible for control of Excise related crimes through detection, prevention, investigation, prosecution of offences under the law and prevention of illicit trafficking in Narcotic Drugs and Psychotropic Substances under Narcotic Drugs and Psychotropic Substances Act, 1985.

To handle these functions, the Department has a chain of functionaries both at its Headquarters at Hyderabad and field formation as detailed below.

¹ One case is = 9 liters



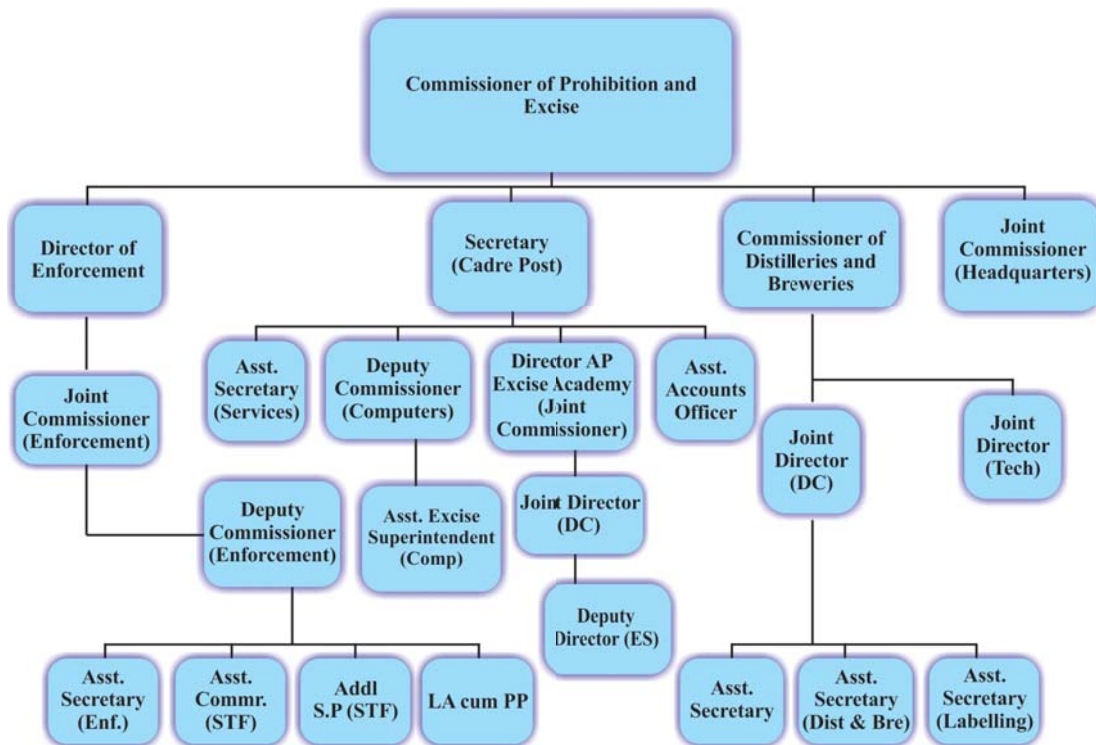
1.5 Organisational set up

1.5.1 Headquarter structure

The Department is headed by the Commissioner of Prohibition and Excise (Commissioner) who is responsible for the overall supervision of the excise revenue management. He is assisted by Commissioner of Distilleries and Breweries, Director of Enforcement, Secretary and Joint Commissioner at Headquarter level. An Assistant Accounts Officer deputed from Treasury and Accounts Department who is also the Drawing Officer assists the Commissioner in financial matters.

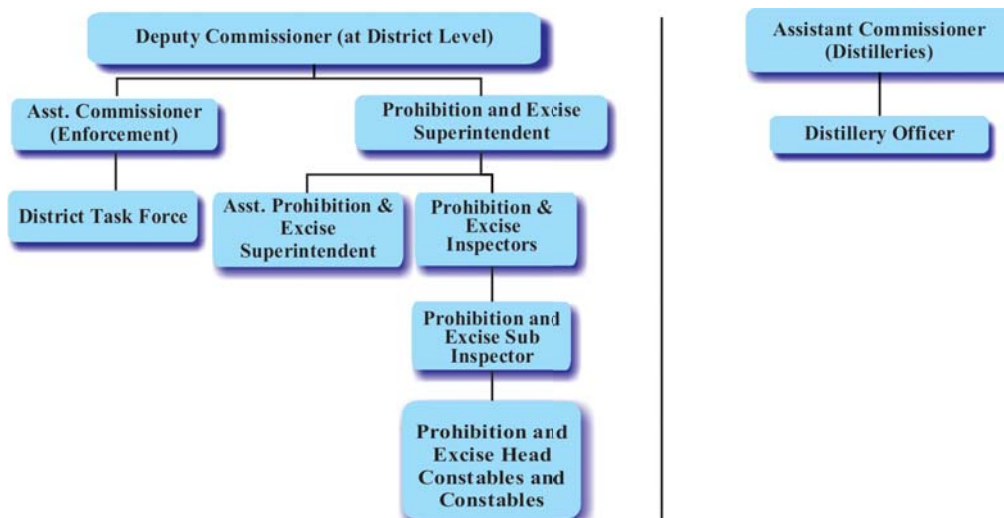
The Principal Secretary, Revenue is the overall in charge of Excise Department at the Government level.

The organisational structure at the Headquarters level is given below:



1.5.2 Field formation structure

For the purpose of effective administration, all the 23 districts of the State are divided into 53 excise districts. Each of the excise districts is under the charge of Prohibition and Excise Superintendent (P&ES) who is assisted by Assistant Excise Superintendent and other staff. Prohibition and Excise Inspectors are in charge of Excise Stations and Check Posts. 23 Deputy Commissioners (DC) and Assistant Commissioners supervise the overall functioning of the Excise Superintendents' offices. There are eight Regional Chemical Laboratories spread out throughout the State under the control of the respective DC.



1.6 Audit Methodology and Scope of Audit

Our audit involved verification of various regulatory requirements of the core activity of the Department, which relate to quantities and values of 'excisable goods' procured, processed, transported and sold principally within the chain, commencing with the raw material i.e. molasses and ending with IMFL. We conducted audit on the basis of records/information to the extent made available by the selected auditee units.

We scrutinised the records of the selected sugar factories, distilleries and the Commissioners' offices at Headquarter and field formations for the period 2005-06 to 2009-10 between September 2009 and January 2011 using various sampling/selection criteria as detailed below. For the purpose of comparison of auctions, records relating to auction cycle 2010-12 were also referred to in certain cases.

Sl. No.	Audit unit	Population	Sample size	Per cent	Method of sampling/ Selection criteria
1.	District	23	17	74	Stratified sampling on the basis of revenue consideration
2.	Sugar factories	35	6	17	Production consideration and risk perception
3.	Primary Distilleries	26	6	23	
4.	IMFL Distilleries	29	11	38	Revenue consideration and risk perception
5.	Prohibition & Excise Superintendent offices	53	19	36	
6.	Assistant Commissioner (Enforcement)	23	2	9	Random selection
7.	Assistant Commissioner (Distilleries)	5	1	20	
8.	Deputy Commissioner	23	5	22	
9.	Apex offices	3	3	100	

Source: As per stratified sampling.



1.7 Audit objectives

The audit was taken up with the objectives of ascertaining as to;

- Whether the Department could perform its dual role of enforcing prohibition and procuring revenue through regulation of liquor efficiently and effectively;
- Whether the provisions and the system of regulating levy and collection of excise duty and other applicable taxes in manufacture of raw material (molasses and rectified spirit) for manufacturing liquor were adequate and they were complied with;
- Whether the provisions and the system of regulating levy and collection of excise duty and other applicable taxes in manufacture of liquor and allotment of licenses for sale of liquor were adequate and they were complied with; and
- Whether there was an adequate monitoring and control mechanism for preventing and detecting revenue leakage and associated crime.

1.8 Audit Criteria

The following Central and State Laws and the Rules made thereunder are to govern the levy and collection of excise duties and other excise receipts like fees, fines etc.

Acts

1. The AP Excise Act, 1968
2. The AP Prohibition Act, 1995
3. The Narcotic Drugs and Psychotropic Substances Act, 1985
4. The Medical & Toilet Preparation (ED) Act, 1955 is a Central Act governing alcohol used in medicines and toilet preparations and receipts are collected by the State.

Rules

1. AP Excise (Grant of License of Selling by Bar and Conditions of License) Rules, 2005
2. AP Excise (Lease of Right of Selling by Shop and Conditions of License) Rules, 2005
3. AP Excise (Grant of license of selling by in-house and conditions of license) Rules, 2005
4. AP Distillery (Manufacture of IMFL other than Beer and Wine) Rules, 2006
5. AP Distilleries (Manufacture of Spirits) Rules, 2006
6. AP Winery Rules, 2006
7. AP Excise (Possession, Import, Export, Transport of Molasses- Conditions of License) Rules 2008.





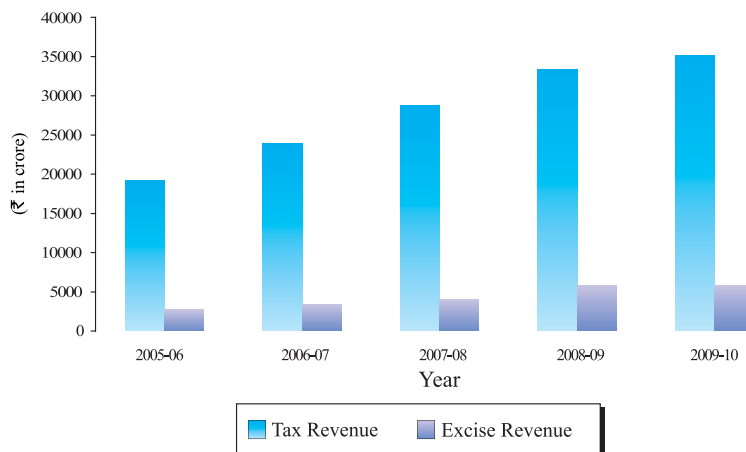
1.9 Trends of revenue

The total tax revenue and State Excise Revenue raised by the Government of Andhra Pradesh during the years 2005-06 to 2009-10 and percentage of State excise revenue to that of the total tax revenue is as mentioned below:

(₹ in crore)						
Sl. No.	Particulars	2005-06	2006-07	2007-08	2008-09	2009-10
1.	Total Tax revenue of the State	19,207.41	23,926.20	28,794.05	33,358.29	35,176.68
2.	State Excise Revenue	2,684.57	3,436.63	4,040.69	5,752.61	5,848.59
3.	Percentage of increase over previous year	28.28	28.01	17.58	42.37	1.67
4.	Percentage of State Excise as part of total tax revenues	13.97	14.36	14.03	17.24	16.62

Source: Figures taken from AP Budget.

The following chart depicts the share of excise revenue in the total tax revenue of the State.



It can be seen from the above table that during 2007-08 there was a decline in excise revenue by 17.58 per cent as compared to 28.01 per cent in 2006-07 but it increased to 42.37 per cent in 2008-09. However, in 2009-10 the revenue declined by 1.67 per cent.

1.9.1 Analysis of tax structure

The key challenge in taking a decision for the Department to prohibit liquor consumption or otherwise is striking a balance between the responsible vending of liquor and maintaining sustained revenue earnings. These intimately related objectives are to be kept in mind while determining the tax incidence on potable alcohol in any State.



Considering the potential for its contribution to the exchequer, the State had levied a series of fee/taxes/duties at various stages of the manufacture and sale of Rectified Spirit (RS) and IMFL.

Various taxes levied on the industry in the State and the changing pattern during the period of audit is listed below.

Sl. No.	Fee/Tax/Duty levied	% Change (+/-) from 2005-06 to 2009-10	
a) At the manufacturing stage			
1.	License fee (₹)		
	RS Distilleries (upto 20 lakh BLs ²)	(+) 6.66	
	IMFL Distilleries (up to 20 lakh PLs ³)	(+) 33.33	
2.	Additional license fee (₹) IMFL(per PL)	(+) 200.00	
3.	Label approval fee (₹)	Nil	
4.	Excise duty (₹) (Basic Price per case up to ₹ 400/450)	(+) 4.44	
	(Basic Price per case from ₹ 401 to 700/451 to 600)	(+) 8.57	
	(Basic Price per case from ₹ 701 to 1000/601 to 850)	(+) 3.75	
	(Basic Price per case above ₹ 1000/850)	(+) 19.73	
b) At the vending stage			
1.	License fee (₹)	(For Shops) ⁴	(+) 90.00
		(For Bars)	
		(For population upto 10000)	(+) 174.36
		(10001 to 50000)	
		(50001 to 300000)	(+) 140.32
		(300001 to 700000)	(+) 123.78
		(above 700000)	(+) 105.93
4.	Margin and special privilege fee of APBCL (%) (2005-06 Basic price ₹≤400) (2009-10 Basic price ₹≤300)	(+) 18.75	
	(Basic price ₹>700 ≤1000)	(-) 4.54	

Source: Figures obtained from Notifications and GOs issued by the Government from time to time.

Apart from the above taxes and duties VAT @ 70 per cent was levied.

² Bulk litre refers to any liquor with a particular proof strength which may be either underproof or overproof.

³ Proof litres corresponds to any quantity of liquor with a strength of 100° proof which is the base standard for determining and expressing one strength of liquors of above 100° or below 100° corresponding to overproof and underproof respectively.

⁴ Biennium system of auction was introduced since the lease year 2006-08.





1.10 Budgeting

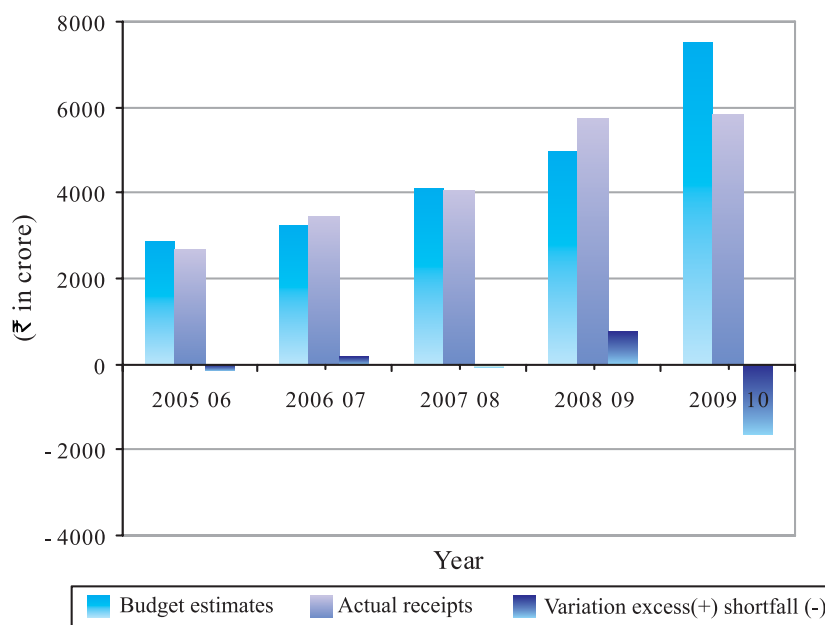
As indicated in the succeeding para 1.12, most of the revenue is received from the licensing of IMFL outlets. Since 2006-07, the Department had switched over to biennial auction of IMFL sales outlets. While there is no separate budgeting exercise, the Department revises (upward) the license fee of the outlets by certain percentage over the revenue received during the previous budget year(s).

The Andhra Pradesh Budget Manual stipulates that the estimates should take into account only such receipts including arrears, which are expected to be actually realised during the budget year.

The variations between the budget estimates and actuals of revenue receipts for the years 2005-06 to 2009-10 is as under:

(₹ in crore)				
Year	Budget estimates	Actual receipts	Variation excess (+) shortfall (-)	Percentage of variation
2005-06	2,851.18	2,684.57	(-) 166.61	(-) 5.84
2006-07	3,250.00	3,436.63	(+) 186.63	(+) 5.74
2007-08	4,125.00	4,040.69	(-) 84.31	(-) 2.04
2008-09	4,991.25	5,752.61	(+) 761.36	(+) 15.25
2009-10	6,260.00	5,848.59	(-) 411.41	(-) 6.57

Source: Figures taken from AP Budget.





Though the Department did not give reply, we infer that the (+) 15.25 variation in 2008-09 was due to increase in actual receipts on account of license fee fetched from the sales outlets consequent on implementation of biannual policy of auctioning.

1.11 Per capita consumption of liquor in the State

The Andhra Pradesh Beverages Corporation Limited (APBCL), a wholly owned Company of the Government of Andhra Pradesh, is conferred with the exclusive privilege of conducting wholesale trade in IMFL. Andhra Pradesh is one of the leading consumers of liquor in the country. The per capita consumption of liquor in the State calculated based on the statistics relating to quantity consumed as furnished by APBCL for the last five years is as follows:

Year	Per capita consumption per annum ⁵	
	Quantity (in litres)	Value (₹)
2005-06	3.77	700.31
2006-07	3.87	722.81
2007-08	1.37	289.15
2008-09	5.09	1,256.43
2009-10	4.47	1,199.31

Source: Figures obtained from APBCL and Directorate of Economics and Statistics.

It may be seen from the above that while there were fluctuations in the quantum of consumption, there had been 71 per cent rise in terms of money spent per head by the consumers on liquor during the last five years.

1.12 Sources of Revenue

Excise revenue is the second largest source of tax revenue for the State which consists mainly of shop rentals, fee for licenses issued to distilleries/breweries and liquor dealers, duty on liquor, taxes and rent on trees and fines and penalties, etc.

Revenue realised by the Department for the last five years from various sources is as follows:

Year	Rentals on country fermented liquor shops/Tree Tax	Duty on				Fines & Confiscation	Other Receipts ⁷	Total
		Duty on		Fines & Confiscation	Other Receipts ⁷			
		Beer	IMFL ⁶					
2005-06	23.35	98.55	2,490.67	7.54	64.46	2,684.57		
2006-07	26.04	132.41	3,207.37	1.43	69.38	3,436.63		
2007-08	34.20	186.88	3,740.11	1.34	78.16	4,040.69		
2008-09	23.56	143.66	5,503.84	3.02	78.53	5,752.61		
2009-10	22.93	154.58	5,578.14	13.01	79.93	5,848.59		
Total	130.08	716.08	20,520.13	26.34	370.46	21,763.09		

Source: Figures taken from AP Budget.

⁵ Calculated as per the population figures furnished by Directorate of Economics and Statistics.

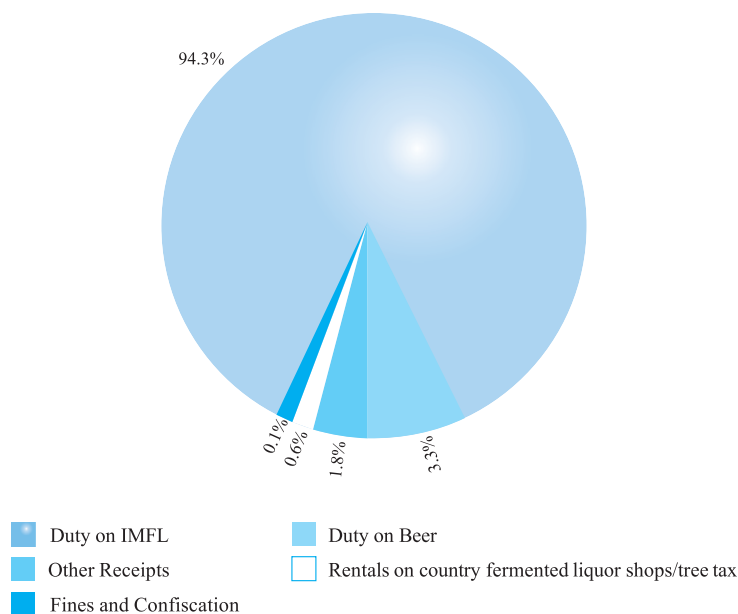
⁶ Includes license fee collected from IMFL sales outlets.

⁷ Includes receipts of commercial denatured spirit, Medicated Wines, Toilet preparation containing alcohol, etc.





The above position is depicted in the following pie chart.



It may be seen from the above that over 94 per cent of the excise revenue is received from excise duty and license fee on sale of IMFL outlets during the five year period. During 2007-08 increase of revenue receipt on account of duty on Beer was probably due to drinking pattern and decline in rentals during 2008-09 was due to reduction of number of toddy shops. Further, continuous declining trend of revenue under the head fines and confiscation during all the years except 2008-09 points to lack of monitoring and control which is discussed in Chapter IV.

1.13 Arrears of revenue

The arrears of excise revenue arise mainly due to default of payment of license fee by the licensees of liquor retail outlets, bars and arrears of earlier years relating to toddy.

The arrears of revenue as on 31 March 2010, amounted to ₹ 50.68 crore (3968 cases) of which ₹ 43.76 crore related to arrears more than five years old. Out of ₹ 50.68 crore, ₹ 0.29 crore (134 cases) only was collected to the end of November 2010 leaving a balance of ₹ 50.39 crore (3834 cases) yet to be collected which include ₹ 1.70 crore (98 cases) collectable in other States. Arrears of ₹ 5.37 crore (138 cases) covered had been stayed by the Honorable Courts and the Government. Demand of ₹ 9.29 crore (1753 cases) was likely to be written off.

The Department had not made any concerted efforts to recover the arrears as only ₹ 0.29 crore were collected against the arrears of ₹ 50.68 crore.



1.14 Organisation of Audit Findings

The audit findings have been organised in four chapters.

- Chapter II deals with the issues pertaining to production of liquor.
- Chapter III points out the issues noted in the processes of licensing and sale of liquor.
- Chapter IV brings out the crucial issues of monitoring and control in tax administration and crime prevention and detection.
- Chapter V gives conclusion of the audit findings and the recommendations.

1.15 Acknowledgement

We place on record our sincere appreciation for co-operation by the Prohibition and Excise Department of the Government of Andhra Pradesh in facilitating our audit. At the outset, an entry conference was held in November 2010 with the Commissioner of Prohibition and Excise and the Commissioner of Distilleries and Breweries and other Departmental officers in which the objectives of the review, audit methodology etc., were explained. The draft review report was forwarded to the Government and Department in April 2011 and discussed in the Exit conference held in July 2011. The Principal Secretary (Revenue) represented the Government, while the Commissioner of Prohibition and Excise represented the Department. Views of the Government/ Department have been suitably incorporated in the report.

