CHAPTER II
DUTY EXEMPTION/REMISSION SCHEMES

The Government may exempt wholly or part of customs duties for import of inputs and capital goods under an export promotion scheme through a notification. Importers of such exempted goods undertake to fulfil certain export obligations (EO) as well as comply with specified conditions, failing which the full rate of duty becomes leviable. A few illustrative cases where duty exemptions were availed of without fulfilling EOs/conditions are discussed in the following paragraphs. The total revenue implication in these cases is ₹ 72.74 crore. These observations were communicated to the Ministry through 12 draft audit paragraphs.

2.1 Export oriented units (EOUs)/Export processing zones (EPZs)/Special economic zones (SEZs) scheme

2.1.1 Export proceeds realisation

Under paragraph 6.12 (d) of the FTP 2004-09, the export proceeds have to be realised within 12 months of exports. The guidelines for monitoring the performance of Export oriented units (EOU)/Software technology park (STP) issued vide Appendix 14-I-G of the HBP, Vol. I, 2004-09, prescribes that it is the responsibility of the Development Commissioner (DC) to monitor realisation of foreign exchange/remittance of EOUs in coordination with RBI.

We observed a few instances where the Development Commissioners did not initiate any action on certain EOUs that were not realising the export proceeds as per the quarterly/annual performance reports within the period prescribed. The details of the cases are tabulated below:-

S. No.	Name of EOU	Period of exports	Foreign exchange remaining unrealised	Duty attributable to unrealised export proceeds	Reply of the department
1.	M/s Suzlon Energy Ltd., Daman Commissionerate	May 2007 to October 2008	₹ 292.58 crore	₹ 3,519.73 lakh	Department reported (June 2011) that ₹ 292.58 crore had since been realised.
2	M/s Computer skill Ltd., Gandhi Nagar, Commissionerate-III, Ahmedabad	July 2006 to September 2006	US$ 6,38,089	₹108.88 lakh	Department forwarded (April 2011) the reply of RBI stating that action is being taken to expedite the realisation of pending exports proceeds.
3.	M/s Comstar Automotive Technologies (P) Limited, M.M. Nagar, Chennai, MEPZ	December 2005 to November 2008	₹ 221.22 lakh	₹ 21.44 lakh.	The Deputy Commissioner, MEPZ in their reply (March 2010) stated that SCN has been issued to the unit. Further, progress was awaited.
	Total			**₹ 3,650.05 lakh**	

The balance export proceeds remained unrealised as of now (January 2012).

We reported (November 2011) the matter to the Ministry; its response had not been received (January 2012).

2.1.2 Non levy of additional duty of customs on DTA clearances

According to the proviso to serial no.2 of the notification no.23/2003-CE dated 31 March 2003 as amended, it is stipulated that while calculating the aggregate of the customs duties, additional duty of customs leviable under sub section 5 of section (3) of the Customs Tariff Act shall be included, if the goods cleared into Domestic Tariff Area (DTA) are exempt from payment of Sales Tax (ST) or Value Added Tax (VAT). Further, in terms of notification no.19/2006-cus dated 1 March 2006, an additional duty of customs shall be levied at the rate of four per cent ad valorem on all the imported goods. Thus, in the case of finished goods cleared in DTA which are exempt from payment of ST or VAT, the special additional duty of customs at the rate of four per cent becomes leviable.

M/s Micro Ink Ltd., (100% EOU) under Central Excise Commissionerate, Vapi, engaged in manufacture and export of goods falling under chapters 28, 32, 34 and 38 of the Customs Tariff had made DTA clearances between 1 March 2006 and 31 March 2009 to its sister units. The DTA clearances made to sister units were treated as 'stock transfer' and cleared under notification no. 23/2003-CE without payment of excise duty equivalent to the four per cent additional duty of customs on the plea that goods cleared in DTA are not exempt from payment of ST/VAT. This resulted in non levy of additional duty of customs amounting to ₹ 19.90 crore.

When we pointed this out (January 2010), the department did not accept the audit observation and stated (February 2010) that sales tax was not paid for clearances to its sister units as it was stock transfer/branch transfer. The department further stated that the goods transferred to sister units were used for their own production and final products are cleared on payment of appropriate taxes. The reply of the department is not acceptable as:

1. The notification no. 23/2003-CE does not provide any specific exemption to 'stock transfer'. It provides exemption only to 'DTA clearances', that too where the goods suffered ST/VAT.

2. Board circular no. 38/2003-cus dated 6 May 2003 had clarified that 'stock transferred' by an EOU to DTA are covered under DTA sale.

3. 'Stock transfer' is covered under the meaning of 'sale' as defined in section 2 (h) of the Central Excise Act, 1944.

However, the department subsequently adjudicated (December 2010) the demand for ₹ 33.14 crore for period upto 30 June 2010.

When we reported (July 2011) the matter; the Ministry stated (January 2012) that the unit had filed an appeal with High Court of Gujarat against CESTAT order of April 2011 directing it to deposit ₹ 11 crore. Mean while, the High Court of Gujarat had passed an interim order (July 2011) directing that the

appeal before CESTAT should not be dismissed by the Appellate authority on the ground of non deposit of statutory amount. Further progress was awaited.

Recommendation

Department may introduce suitable mechanism in the notification itself to levy special additional duty on firm on clearances of goods on stock transfer basis to their related firms if sales tax/VAT is not paid at the time of clearance of goods from customs bonded warehouse.

Incorrect reimbursement of Central sales tax (CST)

As per paragraph 6.11 (c) of the FTP 2004-09, EOUs are entitled to full reimbursement of Central Sales Tax (CST) on purchases made from DTA for production of goods. In terms of clause 2 (a) of Appendix 14-I-I of the Hand Book of Procedures (HBP) Volume-1, admissibility of the reimbursement is subject to the condition that the supplies from DTA must be utilised by the EOU for production of goods meant for export and/or utilised for export products. However, provision of Appendix 14-I-1 was amended in the FTP 2009-14, w.e.f August 2009, removing the compulsion of goods for export and allowing reimbursement of CST to EOUs on supplies from DTA provided these were utilised by the EOUs for production of goods/services.

2.1.3 M/s Sanghi Spinners India Ltd and 20 other EOUs under the Development Commissioner, VSEZ, Visakhapatnam were granted reimbursement of CST amounting to ₹ 21.20 crore on raw materials/consumables procured and utilised by the assessee in production between 2003-04 and 2008-09. However, these units also sold goods valued for ₹ 1503.59 crore in DTA during this period before August 2009, (i.e. date of effect of amendment in the FTP), in addition to physical exports of ₹ 12162.32 crore. Reimbursement of CST on the goods sold back in DTA instead of restricting it to export production resulted in excess reimbursement of CST of ₹ 2.86 crore.

When we pointed this out (November 2010), the VSEZ authorities stated (March 2011) that EOUs were entitled to full reimbursement of CST paid by them as per paragraph 2 of Appendix 14-1-1. The department further stated that there was no restriction for reimbursement of CST in proportion to the value of inputs used in export production.

The reply of the department is not acceptable. The position cited by the department had become applicable only from August 2009 i.e. after the amendment in FTP 2009-14. Prior to that, CST reimbursement was available only for exported goods.

We reported (July 2011) the matter to the Ministry; its response had not been received (January 2012).

2.1.4 We observed that reimbursement of CST was permitted to five EOUs by DC, Madras EPZ on raw materials/consumables procured and utilised in the entire production which included finished goods sold in the DTA during the period April 2006 to March 2009. The reimbursement of CST on the inputs utilised for products sold in DTA was irregular. The excess

reimbursement of CST amounting to ₹ 28.99 lakh was recoverable as detailed below.

Name of the EOU	Excess CST reimbursed (₹ in lakh)
Lucas TVS	1.36
ICIL	3.08
Whirlpool	0.67
Cooper Bussmann	0.02
Comstar Automotive Technologies Pvt Ltd	23.86
Total	**28.99**

We pointed this out to the department in October/November 2009 and March 2010, their reply had not been received (January 2012).

We reported (November 2011) the matter to the Ministry; its response had not been received (January 2012).

2.1.5 Short levy of excise duty on DTA clearances

As per serial no. 3 of the table annexed to notification no. 23/2003-CE dated 31 March 2003 read with condition 3 (i), if the goods cleared by a 100 per cent EOU in DTA are manufactured wholly from the raw materials manufactured in India, it will be liable to pay duty equal to excise duty leviable under section 3 of the Central Excise Act, 1944 and in case the unit uses the imported raw materials, excise duty equal to aggregate of duties of customs is payable as provided at serial no. 2 of the notification ibid. Further, in notification no. 23/2003-CE an explanation-II was inserted from 6 September 2004 vide notification no.46/2004-CE which provided that in case the EOU procures the goods from any other EOU/STP/EHTP the same will be treated as 'imported goods'. In addition to the above 'procurement of goods under benefits of deemed exports under paragraph 8.3 (a) and (b)', were also included vide notification no. 29/2007-CE dated 6 July 2007.

Audit noticed that M/s Phthalo Colours (I) Ltd., Unit-I (EOU), under the jurisdiction of Central Excise Commissionerate, Daman, during 2006-08 cleared its finished goods (Copper Phthalo Cyanine Blue & others) in DTA on payment of Central Excise duty under serial no.3 of notification no. 23/2003. It was however, observed that the raw materials (Phthalic Anhydride, Copper Cathode, Ammonium Molybdate) were procured indigenously either from other EOU (M/s I.G. Petrochemicals) or against advance authorisation of M/s Sterlite Industries & M/s Inwac Metals & Chemicals. Since, the procurement of goods from an EOU or against an advance authorisation are treated as 'imported goods', the unit was required to pay excise duty under serial no. 2 of aforesaid notification no. 23/2003. This has resulted in short levy of excise duty of ₹ 1.88 crore.

When we pointed this out (November 2010), the department partially accepting the observations stated (December 2010) that the unit was required to pay duty of ₹ 70.94 lakh only w.e.f. 6 July 2007 onwards, as the amendment to explanation II of the notification no. 23/2003 was made by notification no. 29/2007-CE effective from 6 July 2007.

Reply of the department is not acceptable because the provisions for treatment of the goods procured from an EOU to be treated as 'imported goods' was

originally inserted in the notification no.23/2003-CE vide notification no. 46/2004-CE dated 6 September 2004 which was further amended vide notification no. 29/2007-CE dated 6 September 2007 which merely included the provisions for treatment of goods received from DTA under benefits of deemed exports as 'imported goods' under the provisions of FTP.

When we reported (November 2011) the matter; the Ministry stated (January 2012) that SCN cum demand notice for ₹ 1.88 crore has been issued to the unit. Further progress was awaited.

Ineligible DTA sales

As per paragraph 6.8 (a) of Foreign Trade Policy (FTP) 2004-09, an EOU may sell goods in the DTA, upto 50 per cent of the value of its exports at concessional rate of duties subject to fulfilment of positive Net Foreign Exchange Earning (NFE). Within this entitlement, an EOU may sell in the DTA, its products similar to goods which are exported from the unit. DTA sale beyond this entitlement is permissible only on payment of full duties. Notification no. 23/2003-CE dated 31 March 2003 specifies the extent of duty concessions available on such DTA sales. Further as per paragraph 6.15 (a) (ii) unutilised imported/indigenously procured goods may be disposed off in the DTA by EOUs with the approval of customs authorities on payment of applicable duties.

2.1.6 M/s Renshell Exports Pvt. Ltd.**,** was granted (November 1998) a letter of permission (LOP) by Development Commissioner (DC), Falta Special Economic Zone (FSEZ) for manufacture and export of 'Aleuritic Acid and seedlac'. The unit made DTA sales of 'Golden seedlac' (₹ 980.64 lakh), Seedlac (₹ 451.23 lakh), '3 percent Seedlac' (₹ 96.53 lakh) during the year 2006-07, 2007-08 and 2008-09 respectively.

Audit scrutiny revealed that the unit had exported 'Aleuritic acid' only during these periods. Accordingly, it was not entitled to DTA sales of 'Golden Seedlac' and 'Seedlac' at concessional rate of duty. This had resulted in short levy of ₹ 58.58 lakh on concessional DTA sales.

When we pointed this out (October 2010), the DC of Central Excise, Asansol-II Division while admitting the observation reported (June 2011) that a protective demand notice for ₹ 41.15 lakh pertaining to DTA sales made during the year 2006-07 and 2008-09 has been issued. As regards DTA sales made during 2007-08, the DC stated that demand notice is being issued. Further progress had not been furnished (January 2012).

2.1.7 As per paragraph 6.6 (e) of the Handbook of Procedures (HBP) -Vol.-I, one of the conditions for import of duty-free inputs by an EOU is that the consumption of inputs shall be based on the Standard Input Output Norms (SION), provided that:

(a) where no SION have been notified, generation of waste, scrap and remnants upto 2 percent of input quantity shall be allowed, and

(b) where additional items other than those given in SION are required as inputs or where generation of waste, scrap and remnants is beyond 2 percent of input quantity, use of such inputs shall be allowed by the jurisdictional Development Commissioner (DC) within a period of three months from the date of and based on self-declared norms, with the Unit undertaking to adjust

self-declared/ad-hoc norms in accordance with norms as finally/fixed by Norms Committee in the Director General of Foreign Trade (DGFT).

Further, as per notification no. 52/2003-cus dated 31 March 2003, as amended, failure to adhere to these provisions would attract levy of duty on such inputs and interest thereon till the date of payment of duty.

M/s Renshelll Exports Pvt. Ltd., during the year 2008-09, made duty free imports of 'Sticklac' valuing ₹ 1.23 crore and processed it to produce '3 per cent Seedlac', which was partly consumed for production of 'Aleuritic Acid' and partly sold in the DTA. The wastage generated during production of '3 per cent Seedlac' from 'Sticklac' was 25 per cent and during production of 'Aleuritic Acid' from '3 per cent Seedlac' was 88 per cent.

However, neither is any SION notified for the manufacture of 'Seedlac' (for which the input 'Sticklac' was imported), nor is 'Sticklac' included as an input for manufacture of 'Aleuritic Acid' as per SION serial no. A1248. Besides, the wastage generated was in excess of the prescribed limit of 2 per cent. Therefore, for import of the input 'Sticklac', the EOU was required to get ad-hoc norms fixed from the jurisdictional DC. But the Unit neither declared any norms, nor applied for fixation of norms by executing undertaking as required under the provisions of the HBP. Therefore, grant of duty exemption on import of 'Sticklac' was irregular, for which customs duty and interest amounting to ₹ 8.68 lakh was recoverable from the unit as per the aforesaid customs notification.

When we pointed this out (October 2010), the DC of Central Excise, Asansol-II Division while admitting the objection reported (June 2011) that a demand notice was being processed for issue to the unit. Further progress had not been furnished (January 2012).

We reported (November 2011) the matter to the Ministry; its response had not been received (January 2012).

Short levy of duty on DTA sale

2.1.8 M/s Magnum Forge & Machine Works Ltd., under Pune III Commissionerate, was issued LOP for manufacture of 'various types of alloy steel forging, valves/component for Oilfield Exploration Equipment'. The unit had cleared waste/scrap in DTA worth ₹ 2.18 crore during the period 2005-06 to 2007-08 and paid Central excise duty at the rate of 16 per cent and education cess at the rate of 2 per cent at the time of clearance in DTA under notification no. 23/2003 dated 31 March 2003 (serial no. 3) as if, the goods are produced or manufactured wholly from the raw material produced or manufactured in India. Scrutiny of Annual progress reports (APR) revealed that unit was utilizing imported raw material as well as indigenous materials for manufacturing the finished goods. Therefore, scrap cleared in DTA also contained scrap generated from imported raw material used during the manufacturing process of finished goods. Hence, clearance of scrap in DTA was to be assessed under serial no.2 instead of serial no. 3 of notification no. 23/2003 and on which custom duties of ₹ 9.69 lakh are leviable.

When we pointed this out (January 2010), the department stated (March 2011) that the unit for sale of scrap had paid duty which was on the higher side against aggregate of Customs and Central excise duty.

Reply of the department is not acceptable because the unit had used both imported as well as indigenous input material for manufacture of finished goods and scrap generated during manufacture which was sold in DTA on payment of excise duty instead of aggregate duties of customs as provided in serial no. 2 of notification no. 23/2003-CE.

We reported (November 2011) the matter to the Ministry; its response had not been received (January 2012).

Anti-dumping duty not collected on DTA sale

Under section 30 of the SEZ Act, 2005, an SEZ unit shall clear its products into DTA after paying the applicable duties of customs including anti-dumping duty under the Customs Tariff Act, 1975 where applicable, as leviable on such goods when imported. Components of Compact Fluorescent Tubes (CFT) and Compact Fluorescent Lamps (CFL) of Chinese origin, when imported and cleared as such by an SEZ unit to DTA, are liable to anti-dumping duty in terms of notification no. 126/2008-cus dated 21 November 2008.

2.1.9 We observed that M/s Gupta Infotech, a unit in Falta SEZ, cleared to DTA 2,34,350 pieces of CFL made out of CFT of Chinese origin valued at ₹ 26.13 lakh between 21 November 2008 and March 2009. However, the goods were cleared without levy of applicable anti-dumping duty amounting to ₹18.08 lakh.

When we pointed this out (March 2010), the department stated (September 2010) that though SEZ is considered to be foreign territory for the purpose of revenue, the sale of goods by SEZ unit to DTA unit is not considered as export.

The department reply is not acceptable in view of the provisions of sub section 2A of section 9A of the Customs Tariff Act, 1975 read with section 30 of the SEZ Act, which provides that articles imported by a 100% EOU are not exempted from levy of anti dumping duty, if these were used in the manufacture of any goods that are cleared into the DTA. In such clearances anti dumping duty is to be levied on that portion of the article so cleared or so used as was leviable when it was imported into India.

We reported (November 2011) the matter to the Ministry; its response had not been received (January 2012).

Recommendation
Department may introduce a specific provision for levy of anti dumping duty for such clearances by SEZ units as it was existing in case of EOUs.

2.2 Advance licence scheme

Delay in taking penal action

Under the Advance authorisation scheme, an importer is allowed duty free import of inputs, which are utilized in manufacturing products for export. The advance authorisation holder has to undertake an export obligation either in value or in quantity terms, as specified in the advance authorisation. The export obligation is required to be fulfilled within 24 months from the date of issue of licence. This was enhanced to 36 months in February 2009.

As per paragraph 4.24 of HBP (Vol.-I), 2004-2009, authorisation holder shall, within two months from the date of expiry of Export Obligation (EO) period, submit to concerned Regional licensing authority (RLA) requisite evidence for discharge of EO. In case he fails to complete EO or fails to submit relevant information/documents, RLA shall take action by refusing further authorisations, enforce condition of authorisation and undertaking and also initiate penal action as per law.

We found some instances where the advance authorisation holders had failed to fulfil the export obligation. Although the department was aware of the shortfalls in meeting the EO, it had not taken penal action. The cases are narrated below:

2.2.1 The test check of records of 11 DEEC licences in the RLA, New Delhi in December 2009 revealed that the authorisation holders had not submitted evidence of fulfillment of EO long after expiry of the prescribed period.

The defaulter orders were issued only in six cases pertaining to M/s BSMC Power Systems Pvt. Ltd. However none of these cases were finally adjudicated. In three out of the remaining five cases, though the SCN had been issued, the department had not taken any further action. In the remaining two cases which pertained to M/s Elin Electronics Ltd, even the SCN had not been issued though export obligation period had expired in July 2005.

After we pointed this out (December 2009), the RLA, New Delhi informed that in six cases of M/s BSMC Power Systems Pvt. Ltd where defaulter orders had been issued, adjudication was completed in March 2010 and sent for recovery.

In the three cases where SCN had been issued, in one case (M/s Teletube Electronics Ltd.), the licencee had submitted export documents in 2009. In another case (M/s Schnieder Electric India Ltd.) the licencee was declared a defaulter (May 2010) and given seven days time to submit documents. In the remaining one case (M/s Aksh Opti Fibres), no reply was received.

In two cases (M/s Elin Electronics Ltd) where SCN had not been issued, the department informed that after the SCN was issued in March 2010, the licensee surrendered the unutilised authorisations.

It was evident that there was undue delay in taking action where the authorisation holders had not fulfilled export obligation.

When we reported the matter to the Ministry, the DGFT, New Delhi accepting the facts stated (January 2012) that the process of monitoring in respect of M/s Schneider Electric India (Pvt.) Ltd., and M/s Aksh Opti Fibress was yet not complete. Further progress was awaited (January 2012).

2.2.2 According to Customs notifications issued from time to time, the importer at the time of clearance of imported material is required to execute a bond/BG with the Customs department to pay on demand an amount equal to duty leviable. The HBP (Vol.-I) 2004-09, also provides that in case of bonafide default in fulfillment of EO, the authorisation holder shall pay to Customs department, customs duty on unutilised value of imported material along with interest.

Audit scrutiny revealed that in 37 advance authorisations issued for CIF value of ₹ 23.66 crore and registered at custom houses located in Delhi, the authorisation holders were required to fulfil EO of ₹ 38.72 crore, as prescribed in the licences. The authorisation holders executed bonds for ₹ 11.32 crore, equivalent to duty foregone amount. Against these authorisations, inputs for CIF value of ₹ 17.28 crore were imported which involved duty forgone amount of ₹ 7.25 crore. In all these cases EO period had expired. As per provisions of the above rules, the customs authorities in these cases were required to initiate enforcement of bonds to recover duties. However, no such action was taken.

After we pointed this out, the department stated (May 2010) that SCN had been issued in 28 cases. It also informed that in most cases export related documents would have been submitted to DGFT and that Export Promotion Monitoring Cell was created in November 2009 to monitor this aspect.

This indicates that there is a requirement for better coordination between the Customs department and the RLA so that timely action could be taken.

We reported (November 2011) the matter to the Ministry; its response had not been received (January 2012).

2.3 Duty entitlement pass book (DEPB) scheme

The objective of 'Duty entitlement pass book scheme' (DEPB) is to neutralise incidence of customs duty on import content of export product. Neutralisation is provided by way of grant of duty credit against export product. This credit could be utilised for payment of customs duty on imported goods except capital goods. As per paragraph 4.3.1 of FTP (2004-09), DEPB credits may be utilised for payment of customs duty for imports made under EPCG scheme also, with effect from 1 January 2009.

M/s National Aluminium Company Ltd., imported (August and September, 2008) three consignments of goods of assessable value ₹ 44.40 crore under EPCG scheme. The department cleared the capital goods on payment of duty partly by cash (₹ 6. 66 lakh) and balance from DEPB credits (₹ 2.22 crore). Since these clearances were made prior to 1 January 2009, utilisation of DEPB credits for imports under EPCG scheme was not permissible. Accordingly, ₹ 2.22 crore was recoverable with applicable interest.

When we pointed this out (October 2009), the department while accepting the audit observation stated (August 2010) that clarification has been sought from the importer regarding goods imported. Further progress had not been furnished (January 2012).

We reported (November 2011) the matter to the Ministry; its response had not been received (January 2012).

2.4 Export promotion capital goods (EPCG) scheme

Non fulfillment of Export Obligation

Paragraph 6.2 of EXIM policy 1997-02, allows import of capital goods at concessional rate of customs duty subject to export obligation equal to 5 times c.i.f. value of capital goods to be fulfilled within a period of eight years from the date of issue of licence. Paragraph 6.11 of HBP Vol-I,1997-02 stipulates that the export obligation is required to be fulfilled blockwise and if export obligation of any particular block of year is not fulfilled in terms of prescribed proportions, the licence holder shall, within three months from the block years, pay duties of Customs on the unfulfilled portion of the export obligation along with the interest.

M/s Tata Elxi Ltd., Bangalore was issued (January 2003) a EPCG licence by RLA, Bangalore with c.i.f. value of ₹ 3.01 crore for export of goods valued at ₹ 15.03 crore. Against import (January/February 2003) of capital goods worth ₹ 55.64 lakh, the licencee failed to fulfil block wise EO, till the expiry of seven years from the date of issue of licence. Accordingly, it was liable to pay customs duty foregone on imports amounting to ₹ 22.15 lakh alongwith interest.

This was pointed out to the department in November 2010; their reply had not been received. However, audit subsequently noticed that the RLA twice directed (November 2010, January 2011) the licencee to regularise the non-fulfillment of export obligation and subsequently issued SCN in June 2011.

When we reported (November 2011) the matter; the DGFT, Department of Ministry of Commerce and Industry stated (January 2012) that the licencee had fulfilled Export Obligation to the extent of 71 per cent (₹ 2.14 crore) and has been advised to submit Foreign Inward Remittance Certificate (FIRC) copy and also complete documentation formalities. The DGFT further stated that development in the case would be intimated.

2.5 Focus product scheme (FPS)

Irregular grant of duty credit

As per paragraph 3.10.2 of Foreign Trade Policy (FTP) 2004-2009, relating to the Focus Product Scheme (FPS), export of notified products (as listed in Appendix 37 D of HBP Vol.-I) were eligible for Duty Credit Scrip equivalent to 1.25 per cent of FOB value of exports for each licensing year, commencing from 1 April 2006. Supplies from Domestic Tariff Area (DTA) units to SEZ

units for which payments were received in free foreign exchange, were also

made eligible with effect from April 2006, vide DGFT notification no. 64 (RE-2007)/2004-2009 dated 24 December 2007. Further, as per serial no. 1 under the Category 'C-Handicraft Items' of Appendix 37D, 'Carpets and other textile floor coverings, knotted (hand knotted category only)' falling under ITC (HS) 5701, and as per serial no.2, 'Carpets and other textile floor coverings, woven (hand woven category only)' falling under ITC (HS) 5702, were among the goods eligible for benefit under the Scheme.

In January 2008, the Office of the Zonal Jt. DGFT, Kolkata issued five FPS Duty credit scrips each to the DTA units M/s Roto India Enterprises and M/s Exotica International, valuing ₹ 54.43 lakh and ₹ 49.95 lakh respectively, for supplies of knotted and woven Carpets and Floor Coverings to three units in Falta SEZ. However, out of 16 Export bills under which the supplies were made by M/s Roto India Enterprises, in eleven Export bills of 'woven' Carpets/Floor Coverings, involving FPS duty credit amounting to ₹ 35.51 lakh, neither the invoices nor the Export bills or the Final assessment sheet issued by the SEZ Customs authority, showed that the goods were of 'hand woven category'**.** Similarly, out of nine Export bills presented by M/s Exotica International, for five Export Bills of 'woven' Carpets/Floor Coverings, involving FPS Duty Credit amounting to ₹ 30.99 lakh, none of the documents produced indicated that the goods were of the 'hand woven category'**.** Thus, there was irregular grant of FPS duty credit amounting to ₹ 66.50 lakh on supply of 'woven' Carpets/Floor Coverings which were ineligible for such benefit.

When we pointed this out (November 2011), the DGFT, Department of Ministry of Commerce and Industry, New Delhi stated (January 2012) that all the eleven Export bills of M/s Roto India Enterprises objected to were classified under the ITC (HS) classification 57023110 as 'woven' carpets/floor coverings and were passed by the customs authority as 'woven' products only. It was further argued that the said ITC (HS) classification was exclusively for 'Hand Woven' products only.

The Ministry's reply is not acceptable because the ITC (HS) classification and corresponding Customs Tariff Heading 5702 3110 covers 'woven' products, both 'hand-woven' and otherwise, and the Carpets/Floor Coverings in question were indeed assessed correctly by Customs under the said heading as 'woven' only, and not specifically as 'hand-woven'. It was the Licencing authority that had erred in assuming that the heading under which the said goods had been assessed by Customs was exclusively for 'hand woven' products.