

CHAPTER VII

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 fulfill prescribed export obligations (EO) as well as comply with specified conditions, failing which the full rate of duty becomes leviable. During test check (March 2012 to February 2014) of records, a few illustrative cases noticed where duty exemptions were availed of without fulfilling EOs/conditions are discussed in the following paragraphs and 13 cases of duty exemption/remission have been listed in **Annexure 7**. The total revenue implication in these cases is ₹ 182.65 crore.

Served from India Scheme (SFIS)/Focus Product Scheme (FPS)

Grant of excess duty credit of ₹ 58.01 lakh

7.1 Served from India Scheme (SFIS) provides for duty credit at 10 per cent of the foreign exchange earned by the Service Providers in the current financial year for the services listed in Appendix 41 of HBP. However, export of “goods” shall not be entitled for benefits under SFIS (paragraph 3.12.3 of the FTP).

M/s Shriram EPC Ltd., Chennai was granted (September 2012) duty credit scrip for ₹ 396.95 lakh by RLA, Chennai under SFIS Scheme at 10 per cent of the free foreign exchange of ₹ 4050.55 lakh earned during the year 2011-12 for providing “Construction and Engineering related services”, after imposing a late cut of 2 per cent in terms of paragraph 9.3 of the Handbook of Procedures (Vol.I), 2009-14 for delayed submission of application.

Audit scrutiny revealed that as per the self declaration made by the company on 25 August 2012 in respect of the remittances received for rendering of services and as per the Certificate issued by the Chartered Accountant furnished as Annexure to ANF 3B, the Foreign exchange earned during the year 2011-12 was ₹ 3458.59 lakh only. However, while filing the application online it was wrongly mentioned as ₹ 4050.55 lakh (the foreign exchange earned during the previous year 2010-11). As a result, the duty credit of ₹ 396.95 lakh was granted whereas the actual entitlement was ₹ 338.94 lakh only after imposing late cut of 2 per cent. Thus, incorrect reckoning of the free foreign exchange earned resulted in excess grant of duty credit of ₹ 58.01 lakh.

The Assistant Director General of Foreign Trade, Chennai informed (November 2014) that demand notice has been issued to the firm.

Duty credit allowed for ineligible services

7.2 Supreme Court in the case of Tata Consultancy Services Vs the State of Andhra Pradesh (STC Vol.137 of 2004) and in the case of BSNL Vs the Union of India and others (STC Vol. 145 of 2006) upheld levy of Sales Tax on canned software treating them as goods because Copy right of a programme may remain with the originator of the programme but the moment copies are made and marketed, it becomes goods which are susceptible to sales tax. Accordingly, on the analogy of being goods not entitled to duty credit under SFIS.

M/s Kalaingar TV Private Limited was granted duty credit of ₹ 54.71 lakh by RLA, Chennai under SFIS, at 10 per cent of the free foreign exchange earned by them during the year 2011-12 considering the “License fee for supply of video programmes” earned by them through various TV channels abroad as rendering of “entertainment services”.

Since the earnings were on account of transfer of right to use the title or Copy right and not on account of rendering of any service, it could not be reckoned for duty credit under SFIS. This had resulted in irregular grant of duty credit of ₹ 54.71 lakh which was recoverable with interest.

DGFT, New Delhi stated (November 2014) that transmission of programme through satellite communication falls under Srl. No. 2A of Appendix 41 of the HBP under communication Services- Audio visual service and this could not be classified as “Goods” and the “copyright” have not been excluded from the grant of duty credit.

DGFT’s reply may be viewed in the context of the fact that the earnings were on account of transfer of right to use the title or “copyright” and not on account of rendering of service. According to aforesaid judicial pronouncement “copyright” or right to use the title are termed as “goods” under the Sale of Goods Act thus ineligible as service for grant of credit.

Net Foreign Exchange Earnings by Hospitality Sector (Paragraphs 7.3 to 7.24)

7.3 Introduction

The hospitality industry is a broad category within the service industry that includes lodging, event planning, theme parks, transportation, cruise line, and additional fields within the tourism industry. A hospitality unit such as a restaurant, hotel, or even an amusement park consists of multiple groups such as facility maintenance, operations (servers, housekeepers, porters, kitchen workers, bartenders, etc.), management, marketing and human resources. Indian hospitality sector is estimated to contribute between 8-9 percent towards India’s GDP. During the period 2011 to 2013, 19.84 million foreign tourist visited India and total foreign exchange earned was ₹ 279749

crore¹⁷. India ranked 16th in World Tourism receipts with an average share of 1.61 percent. While in Asia and the Pacific region tourism receipts its rank was 8th with an average share of 5.45 percent during the same period.

Growth opportunities in travel & tourism could not be realized without the development of the hospitality sector. Export promotion measures for service sector are mainly covered under SFIS and EPCG scheme. The total duty foregone under these two schemes (including hospitality sector) is shown in table 7.1.

Table 7.1- Duty foregone

				(Cr. ₹)
Duty foregone	2011-12	2012-13	2013-14	Total
EPCG	9672	11218	8990	29880
SFIS	555	590	639	1784
Total	10227	11808	9629	31664

Source: Union Receipt Budget, CBEC DDM

7.4 While announcing highlights of annual supplement 2013-14 of Foreign Trade Policy it was declared that under SFIS scheme, service providers are entitled to duty credit scrips under the scheme at the rate of 10 percent of free foreign exchange earned during a financial year. The entitlement w.e.f 18.4.2013 is to be calculated on the basis of net foreign exchange earned (i.e., after deducting foreign exchange spent from the total foreign exchange earned during the financial year).

7.5 As per policy circular no. 60/97-2002 dated: 24.12.1998 various categories of rupee payments which would be regarded as foreign exchange earned for the purpose of EPCG scheme are:-

- Payment received from foreigners in Indian rupees against encashment certificate.
- Payment received in Indian rupees from travel agents/tour operators earned from hotel stay of foreign tourist (considered as foreign exchange under section 80HHD of Income Tax Act).
- Payment received by (a) air/flight catering unit, stand alone and others and (b) by hotels for staying of foreign airline crew from foreign airlines in Indian rupees against their repatriable earnings.
- Payment received in Indian rupees, from diplomats, embassies, UN organization out of their convertible foreign exchange.

¹⁷ Source:- India tourism statistics at a glance- 2011, 2012 & 2013, Ministry of tourism, GOI

The foreign exchange earned through money changers licence (not against hotel bills) shall not be treated as foreign exchange earnings for the purpose of EPCG scheme. In respect of the above services, the licence holder shall be required to submit a CA certificate in lieu of certificate from the bank.

7.6 Audit Objective

- Whether the hospitality sector is facilitated by the duty benefits of Foreign trade policy (FTP) under the mainly two schemes; Export promotion Capital goods (EPCG), and Served from India scheme (SFIS), with the objective to earn foreign exchange as per Foreign Trade Policy (FTP) Guidelines.
- Whether the internal control systems and monitoring mechanisms are effective for promoting foreign exchange earnings by the service providers in the hospitality sector.
- Whether the duty credit scrips have been utilized as per the prescribed provisions for import of eligible items relating to the line of business be the entitled service providers such as hotels, restaurants, tour operators etc.

7.7 Audit Coverage

Records were examined of various agencies viz. Regional Licencing Authority (RLA) of DGFT, Customs Ports and Bank involved in administration, implementation and foreign exchange earnings of EPCG & SFIS licences, service providers/beneficiaries in the hospitality sector and EPCG licences issued during 2005-07 (considering the EO period of 6-8 years).

EPCG Licences redeemed during the period 2012-14 and SFIS licences issued during the period for 2012-13 & 2013-14 were examined.

7.8 Audit methodology and sample selection

(i) In case of EPCG, the licences issued during 2005-06 & 2006-07 were selected on the basis of duty foregone, export obligation and foreign exchange earned. EPCG authorizations in which duty saved is ₹ 100 crore or more where the EO period is 12 years were examined separately.

(ii) In case of SFIS, the licences issued during 2012-13 & 2013-14 were selected on the basis of CIF value of duty credit scrips issued to the licence holders against the foreign exchange earnings in the relevant financial year.

(iii) The sample selection was done based on the records made available to audit.

Audit Observations

7.9 Audit observed that duty benefits availed under SFIS & EPCG schemes were to the tune of ₹31664.64 Crore. However, DGFT did not have the segregated figures of benefits availed in the hospitality sector. It has not been captured separately in the DGFT EDI also. Therefore, the impact of this sector and its correlation with the FTP will not be known. The task forces constituted by the DOC also have not considered it necessary to look into the hospitality sector to rationalize its transaction cost. Though the hospitality sector is an emerging sector growing at the rate of 8-9 % of the GDP with FEE to the tune of Rs 279749 Crore (2011-13).

7.10 Internal control & monitoring

We observed that control for avoiding any leakages in revenue generation or misuse of the duty benefits availed were lax. Few cases have been shown below:

7.10.1 Internal controls procedures and internal audit system

DGFT had issued an instruction in January 2000 under which a Post Issue Audit Wing (PIAW) was required to be constituted in all RLAs for the purpose of test audit of five percent of the licences issued for ensuring the veracity of documents submitted along with application. The FTDOs of the sections will generate a list of files on 1 and 16 of every month on random basis by selecting a minimum of 5 percent of files for audit. Accordingly the authorization list for particular section and for particular scheme has to be generated. The sections will verify the genuineness of all the relevant documents submitted like RCMC, BRCs/FIRCs, Shipping Bills/Bill of exports, and registration with different authorities. A separate register as prescribed of circular dated August 2007, be maintained for recording and monitoring the progress of the exercise.

7.10.2 Regional Licensing Authorities (Ahmedabad and Vadodara) were not auditing the selected 5 percent of EPCG/SFIS licence files. Further, cross verification of genuineness of the relevant documents submitted like RCMC, BRCs/FIRCs and registration with different authorities was also not being carried out. A separate register was either not maintained for recording and monitoring the progress of the exercise or wherever maintained, no periodic entries were made. Further, there was no set up of Post Issue Audit Wing (PIAW) at RLA Bangalore also. RLA, Bangalore has intimated (November 2014) about reconstitution of the PIAW.

RLA Ahmedabad stated (June 2014) that specific reply would be furnished after examination of the case. RLA, Vadodara stated that they have selected 5 percent of files on random basis for Post Issue Audit and made a reference to concerned authorities for verification of RCMC, BRC/FIRC, and Shipping Bills/Bills of Exports. A register was also maintained by the department.

Reply of the RLA, Vadodara is not tenable because no Post Issue Audit Wing (PIAW) was set up nor register maintained was as per prescribed proforma. Moreover there was no entry in the register after May 2012.

7.10.3 RLA, Jaipur had issued a show cause notice M/s North West Marwar Resort & Health Spa (P) Ltd on the basis of DRI letter No.840/JPR/19-XVIII/2004/1842 dated 16.11.2005 regarding mis-use of authorizations under EPCG scheme. The matter was also filed in Customs & Central Excise Settlement Commission, Principal Bench, New Delhi in June 2006. As per details available in the files, out of ₹ 120.72 lakh admitted as liability, an amount of ₹ 92.54 lakh was stated to be paid during investigation and ₹ 28.18 lakh was lying pending for recovery.

RLA, Jaipur accepted the audit observation and stated that there was no updated position available in these cases after February 2007. RLA further stated that DRI office would be asked for updated position in those cases.

The fact remains that weak monitoring of the recovery cases has led to postponement of recovery even after lapse of seven years. In all the audit observations, it was amplified that the percentages prescribed for post audit has not been adhered to.

7.11 Lack of co ordination between RLA and Customs / Service tax department

Deficiency/inadequacy in monitoring mechanism in respect of EPCG scheme was observed and highlighted in subsequent paragraphs, SFIS does not involve monitoring since it is a post export scheme but in 12 out of 13 SFIS files examined in audit, no 'statement of imports' as prescribed under Para 3.12.6 of FTP had been submitted by the service providers.

As regards online transmission of licenses as well as transfer of live data relating to imports and exports, EDI system exists for online transmission of licenses and exports between RLA and Customs in case of EDI enabled Ports but it has been observed in RLA Kolkata that there is no system to exchange live data relating to imports. However, in the case of exports of services, particularly services rendered by hospitality sector, there is no involvement of customs department in the transaction (where there is no requirement of filing shipping bills) by such service providers and of RBI on foreign exchange realization. Nor the FE earned by Hospitality Service Sector was mapped with Service Tax Form (ST-3) required to be filled by the service provider or importer of services.

7.12 Improper monitoring and Implementation of EPCG/SFIS scheme

Audit observed at RLA Kolkata that no system in the RLAs to verify (other than by correspondence with the applicants) the correctness of

data/information i.e BRCs and other related documents submitted by the exporter for determining the eligibility under the SFIS/EPCG schemes. Complete reliance is made on the declarations by the service providers of the nature of services provided, and statement of exports certified by the chartered accountants for grant of SFIS duty credit certificates/fixation and discharge of average exports in case of EPCG scheme.

Absence of controls to correlate these declarations with other statutory documents like annual accounts, BRCs, IT returns and foreign inward remittance certificate is a risk area which needs to be looked into. This is more so in case of exports of services of the hospitality sector in which the customs department has no role in the transactions and also where cases of pending foreign exchange, if any, is not reflected in the outstanding statement (XOS) issued by the Reserve Bank of India .

For instance, in case of M/s Parikh Inn Private Ltd., Jamshedpur (RLA Kolkata), it was noticed that the invoices for import of capital goods was addressed to the applicant on behalf of Fortune Hotel Centre point by Welcome Group and the capital goods were installed at the Fortune Hotel as per the certificate issued by chartered accountant.

Similarly, in case of benefit of SFIS granted to M/s Sincere Developers Pvt. Ltd. the service provider was Hotel Radisson Agra, as per FIRCs.

Again, while Hyatt Regency, Kolkata was the service provider, the claim was made by M/s Asian Hotels (East) Ltd.

In all these cases, the relationship between the applicant-claimant and the service provider was not on record. Further, the IEC of the applicant did not show the name of the actual service provider as branches/units of the claimant. In these cases, it was also not clear whether the claimant had earned foreign exchange from business other than that was eligible and admissible as per the provision under the schemes. The department does not have the mechanism to track whether the benefit under the schemes is being availed by the actual users/licence holders.

7.13 Foreign exchange actually realized vis a vis export

DGFT did not have aggregated information of the foreign exchange actually realized by the hospitality sector with respect to the services provided. This would have been a reliable measure to evaluate the success of the scheme with regards to the hospitality sector.

Compliance issues

Audit observed that compliance to the FTP provisions of the EPCG and SFIS schemes are not being adhered to in many cases leading to slippage in FE earnings and grant of undue benefits to the licencees.

SECTION- I (Export Promotion Capital Goods (EPCG))

7.14 Irregular / short fixation of export obligations amounting to ₹110.54 lakh

In case of domestic sourcing of capital goods, export obligation shall be reckoned with reference to notional custom duties saved on FOR value (Para 5.7 FTP).

7.14.1 In two cases (one licence each of RLA, Ahmadabad and Vadodara) the licence holders invalidated their EPCG licences for procurement from indigenous sources and the EO was fixed taking into account the central excise/customs duty applicable on capital goods. It was noticed that non fixation of EO on the basis of notional customs duty resulted in short declaration of duty saved to the extent of ₹ 5.81 lakh and corresponding short fixation of EO to the extent of ₹ 46.49 lakh. Department has also issued EODC for these licences. This has resulted in short fulfillment of Export obligation of ₹ 38.41 lakh.

DGFT, New Delhi stated (January 2015) that RLA, Vadodara has intimated that the firm has submitted revised ANF 5B showing total fulfillment of EO. DGFT further stated that RLA, Ahmedabad had asked concerned exporter to regularize the case. However a copy of the revised document was not submitted for verification by audit.

7.15 Violation of actual user condition

Import of capital goods shall be subject to actual user condition till export obligation is completed (Para 5.4 of FTP).

JDGFT, Trivandrum issued five percent EPCG authorization (Licence No 5330000997 dated 22.09.2006) to M/s Dodla International Ltd, (IEC No 0405007884) with a specific export obligation of ₹ 365.77 lakh for the duty saved amount of ₹45.72 lakh. The licensee imported the capital goods during October 2006 to January 2007 for an actual duty saved amount of ₹ 45.55 lakh but failed to fulfil the prescribed export obligation.

Meanwhile, M/s Oriental Hotels Ltd. intimated (April 2014) JDGFT, Trivandrum that M/s Dodla International Ltd. had leased out the property to them and an application has been filed (September 2010) to the DFGT to transfer the EO of M/s Dodla International to M/s Oriental Hotels Ltd.

EPCG Committee decided (letter No. 01/36/218/151/AM-11/EPCG-I dated 21.12.2011) to allow the transfer of EO imposed against the authorizations issued to M/s Dodla International Ltd to M/s Oriental Hotels Ltd, subject to the condition of submission of fresh Bank Guarantee/ LUT as applicable before endorsement of EPCG licence. Even though two and half years have elapsed, M/s Oriental Hotel Ltd had not executed any BG/LUT in this regard.

DFGT while accepting the fact about non-execution of a fresh BG/LUT by M/s Oriental Hotels Ltd as per decision of the EPCG committee stated (January 2015) that the firm's request for exemption from BG/LUT being a Star Export House is being examined. However, it was further contended that execution of fresh BG/LUT is not relevant at this stage because (i) M/s Oriental Hotels have already executed BG with Customs which will not be released until redemption is allowed by the RLA and (ii) the firm have furnished documents fulfilling the prescribed EO which are under scrutiny. DFGT further added that EPCG committee was considering the transfer of EO and not the EPCG licence.

The DGFT's reply may be viewed in the context of the fact that M/s Dodla International Ltd. was issued EPCG licence and had availed duty benefits but failed to fulfil the prescribed EO, action for which has not been taken by the licencing authority. Later M/s Oriental Hotels Ltd. has gone ahead utilizing the goods imported by M/s Dodla International Ltd. without fulfilling the conditions imposed (fresh BG/LUT) by the EPCG committee and subsequently claimed fulfillment of EO without endorsement of EPCG license in their favour. It is not understood how DGFT is considering transfer of EO to M/s Oriental Hotels Ltd. without endorsement of EPCG licence in their favour.

7.16 Monitoring of export obligation

7.16.1 Non fulfillment of export obligation

The EPCG authorization holder shall fulfil 50 percent export obligation in the block of 1st to 6th year from the date of authorization (Para 5.8 of HBP Vol.I). Where export obligation of any particular block of years is not fulfilled such authorization holder shall, within 3 months from the expiry of the block of years, pay duties of customs along with applicable interest of an amount equal to that proportion of the duty leviable on the goods which bears the same proportion as the unfulfilled portion of the export obligation bears to the total export obligation.

At JDGFT office Varanasi fixed export obligation of ₹ 59.77 lakh was not found to be fulfilled by Mall Hotel Varanasi Cantt (licence No. 1530000229 dated 19.04.2006. Similarly at JDGFT, Trivandrum in two cases evidence of fulfilment of export obligations of ₹420.49 was not submitted even after expiry of EO period.

At RLA Kolkata four EPCG authorizations between August 2005 and January 2006 were issued to two service providers M/s Hotel Hindustan International, Kolkata, (3 nos.) and M/s Speciality Restaurants (P) Ltd. The authorization holders had failed to fulfill the conditions of the authorization, customs duty foregone amounting to ₹15.37 lakh along with interest thereon amounting to ₹18.47 lakh (June 2014) aggregating ₹33.84 lakh stood recoverable. In

another 13 EPCG Authorizations between June 2006 and March 2008 to M/s Hotel Hindustan International and two others for import of various capital goods for duty saved amount of ₹ 85.80 lakh. The authorization holders had not submitted evidence of fulfilment of prescribed EO for the 1st block (50 per cent in 1st to 6th year). It had also not submitted annual progress reports in compliance of Para 5.9.1 of HBP, Vol-I. Therefore, the authorization holders were liable to pay proportionate customs duty foregone (i.e 50 percent of total duty foregone) amounting to ₹ 42.96 lakh and interest thereon.

At RLA Bengaluru, in respect of three cases, it was observed that block wise fulfilment of the obligation of Rs 549.61 lakh was not achieved even after the due date which involved a duty saved amount of ₹ 68.36 lakh. RLA has intimated (November 2014) that SCN has been issued.

DGFT, New Delhi informed (January 2015) that in respect of licence issued by RLA, Varanasi utilization certification from Customs (ICD, TKD) is awaited. RLA, Kolkata have issued letters to the firms for submission of correct FIRC in four licences. RLA, Bengaluru reported that the firms have submitted documents fulfilling the EO in the first block itself in all the three licences.

Audit would like to verify the papers stated to have been submitted regarding cancellation of the licence and fulfillment of EO.

7.16.2 Non submission annual progress report

The EPCG authorization holder shall submit to the licensing authority by 30th April of every year, report on the progress made in fulfilment of export obligation against the licence issued as well as annual average level of exports achieved (Para 5.9.1 of HBP). The report shall be submitted electronically on the DGFT website. The licensing authority may issue partial EO fulfilment certificate to the extent of EO fulfilled in a particular year.

Annual performance reports were neither submitted by the authorization holders nor were insisted upon by the RLAs. RLA, Bengaluru (11 cases), RLA Cochin (15 cases), RLA Trivandrum (4 cases), RLA, Ahmedabad (1 case) and RLA, Jaipur (all licences).

DGFT, New Delhi informed (January 2015) that out 11 cases of RLA, Bengaluru, in 4 cases annual progress reports have not been submitted, however, documents fulfilling the EO have been submitted, SCN has been issued in 1 case, in 3 cases licensees have been asked to furnish the documents, EO has been discharged in 1 case, 1 licence has been surrendered, while in remaining one case firm has completed the EO during 2007-08, accordingly annual report was not required.

In respect of RLA, Cochin (15 cases) it was stated that 12 licences have already been redeemed, EO period was extended up September 2015 in 1 licence, while 2 licencees have been asked to regularize their cases.

In four cases of RLA, Trivandrum it was stated that annual performance report was called for but could not be submitted by the licencees because of non-compilation. However, in 2 cases EO have been fulfilled and licences were redeemed, in another case EO documents submitted are under scrutiny, while remaining 1 case is under adjudication.

RLA, Ahmedabad informed that the licence has been surrendered. Reply from RLA, Jaipur is awaited (January 2015).

The fact remains that cases were not monitored as per the FTP provisions and procedures.

7.17 Incorrect fulfillment of export obligation against duty saved of ₹ 111.02 lakh by non group company

Export obligation shall be fulfilled under EPCG scheme, through direct export by the license holder or through third party (s) {Para 6.5(ii) 1997-2000}. If a merchant exporter is EPCG authorization holder, name of supporting manufacturer shall also be indicated on shipping bills. At the time of export, EPCG authorization number and date shall be endorsed on shipping bills which are proposed to be presented towards discharge of export obligation.

Group Company as defined in paragraph 9.28 of the FTP, means two or more enterprises which, directly or indirectly, are in a position to exercise 26 percent. Or more of the voting rights in the other enterprise; or (ii) appoint more than fifty percent, of the members of the board of directors in the other enterprise, or for the group companies to claim benefits or have their exports counted for benefits to be claimed by another member of the group, the group company should have been in existence at least two years prior to the date of application under any of the export promotion schemes notified in the policy., where license has been issued to any Group Company” the export obligation may also be fulfilled by export of manufactured goods by any other company(s) belonging to such Group Company.

RLA, Bhopal issued EPCG license No.AAAC9739KST001 to M/s Entertainment World Developers Pvt. Ltd., Indore for import of capital goods during the period 2005-06 to 2006-07. The authorization holder fulfilled the export obligation through its group company i.e M/s Flexituff International Ltd. Pithampur. The memorandum and article of association of the company revealed that M/s Flexituff International Ltd. Pithampur was not approved as a group company. It was further revealed that the authorization holder relates to Export of Items under ITC HS Code 94032090 i.e Tourism and Travel-related Services and supporting group co. M/s Flexituff International

Ltd. Pithampur is exporter of HDPE/PP Woven sacks/ Fabrics/PP jumbo bags etc. The licensee neither disclosed its group company during issuance of licenses nor indicated as supporting exporter company in shipping bills, in compliance of EXIM Policy. This resulted in incorrect savings of customs duty of ₹111.02 lakh, liable to be recovered along with interest as per aforesaid Rules and penalty as per Foreign Trade (Development & Regulation) Act 1992.

DGFT, New Delhi citing RLA Bhopal report without furnishing documentary evidence stated (January 2015) that M/s Flexituff International Ltd. is a Group Company of M/s Entertainment World Developers Pvt. Ltd and exports of products manufactured by M/s Flexituff International Ltd. are eligible under para 5.4 (i) of the FTP for fulfillment of EO.

Audit would like to re-examine the issue after receipt of documentary evidence from the department regarding eligibility of Group Company and export obligation imposed over and above the average exports achieved by the group company in preceding three years for both the original and the substitute product(s) as envisaged in para 5.4 (i) of the FTP.

7.18 Delay in issue of export obligation discharge certificate

Regional licensing authority shall ensure disposal of application of redemption of EPCG licence within 30 days. Shortcomings, if any, shall be pointed out in one go (Para 5.13 of HBP). All correspondence, thereafter, shall relate to these deficiencies only. Fresh correspondence, if necessary, shall be made within 15 days. Once documents are complete, EO will be discharged within 30 days of receipt of complete documents/information. In case of failure to fulfil export obligation or any other condition of authorization, authorization holder shall be liable for action under FT (D&R) Act,1992, orders and rules made hereunder, provisions of FTP and the Customs Act,1962 (Para 5.17).

Process of issue of final discharge certificate/rejection shall be completed within a period of 90 days from the date of receipt of initial request. Application that remains outstanding beyond a period of 90 days shall be reported to DGFT along with reasons thereof, immediately thereafter.

At RLA, Jaipur, the audit noticed that in the two cases the export obligation discharge certificate (EODC) was issued beyond 90 days from the date of receipt of application for EODC and no report along with reasons thereof was found sent to DGFT (Table 7.2).

Table 7.2: EODC cases

Sr. No.	Name of Service Provider	Licence No. & Date	Amount of duty saved (lakh ₹)	Date of receipt application for redemption	Date of issue of EODC	Time taken for issue of EODC (in days)
1.	Heritage Inn Pvt. Ltd., Jaipur	1330001112 dated 26.10.2005	11.42	02.09.08	13.05.09	254
2.	Shaina Builders Pvt. Ltd., Jodhpur	1330001178 dated 02.02.2006	11.32	03.08.09	30.11.09	120

RLA Jaipur stated that matter is being examined and reply will be sent.

7.19 SECTION- II Served From India Scheme (SFIS)

7.19.1 Incorrect grant of duty credit scrip amounting to ₹ 7589.49 lakh for promoting foreign brands against objective of SFIS

Objective of SFIS is to accelerate growth in export of services so as to create powerful and unique "Served From India" brand, instantly recognized and respected world over (Para 3.12.1 of FTP).

In this regard, the Policy Interpretation Committee (PIC) vide its minutes of meeting No.09/AM09 dated 27.01.2009 & No. PIC 10/AM-12 held on 27th December 2011, explained the basic objective of SFIS scheme of creating a unique "Served from India" brand and stated that the scheme is essentially for encouraging Indian brands. It was further clarified that the FTP did not intend to incentivize any brand which is created outside India. Such Indian brand should be so unique as to be easily recognizable and create a distinct identity for itself both domestically and internationally. Essentially such a brand should enhance the Indian image and hence the FTP used the phrase "Served from India" brand. The Committee, therefore, concluded that grant of SFIS benefits to companies which represent brands, not identified as Indian brands would not be harmonious with the intent behind the scheme.

Ninety one duty credit scrips were issued by the RLA Mumbai and Pune and 19 scrips by other RLAs (RLA Kolkata-8, RLA Ahmedabad-5, RLA, Jaipur-4, RLA Bengaluru-2) to various service providers using brand names of established foreign brand hotels during 2011-14. This resulted in irregular grant of duty credit scrips in these 110 cases amounting to ₹ 7589.49 lakh.

RLA, Jaipur accepted the audit observation. RLAs Bengaluru and Kolkata stated that FTP never differentiates between Foreign and Indian company in matters related to availing benefits under its schemes including SFIS. Brand name is universal in nature and does not belong to a country. These hotels are owned/ managed by Indian companies which run these hotels in brand name under an agreement with the foreign company, who is the owner of that brand. Accordingly, they are eligible for benefits under the scheme.

The reply of RLAs Bengaluru/ Kolkata were contradictory to the decisions taken by the Policy Interpretation Committees (09/AM09 and 10/AM 12) and may be viewed in the context of the fact that the basic objective of SFIS is to create a unique 'Served from India' brand. Replies from other RLAs were awaited (January 2014).

7.19.2 Incorrect grant of duty credit scrips on earnings in Indian Rupees/Foreign exchange through travel agents

- i. In 55 duty credit scrips of ₹290.50 lakh (RLA, Mumbai-28 cases, ₹ 145.71 lakh, RLA, Goa- 27 cases, ₹144.79 lakh) were irregularly issued to six service providers on earnings in Indian rupees/Foreign exchange through tour operators & travel agents which is recoverable from the licencees.
- ii. RLA, Jaipur issued (December 2012) a Served from India Scheme (SFIS) Authorization for duty credit ₹ 335.46 lakh to Rajasthan Tourism Development corporation Ltd. (RTDC), Jaipur without fulfillment of required conditions. The RTDC was engaged in tour operator services of Palace on Wheels (a joint venture with Indian Railways) and as per agreement (June 2009), RTDC has 44 per cent share whereas Indian Railways has 56 per cent share. Since the Indian Railways was the major shareholder of the joint venture, but the Disclaimer Certificate from them was neither obtained and nor submitted with the application. Application submitted by RTDC revealed that total Foreign Exchange earned during 2011-12 was shown ₹ 3354.61 lakh which includes ₹ 2448.58 lakh earned by other Travel Agents and only ₹ 906.03 lakh was earned directly by RTDC. Foreign Inward Remittance Certificate was also not found submitted. In spite of these deficiencies RLA has accepted the application and issued authorization under SFIS, which resulted in irregular grant of duty credit scrip of ₹ 335.46 lakh.

RLA, Jaipur justified (April 2014) the claim on the grounds that RTDC exclusively is organizing the joint venture and the foreign exchange earned was directly deposited in their account, which was subsequently paid to Indian Railways. Further, RLA reiterated that travel agents who receive foreign exchange earnings were also entitled for SFIS and also stated that as per Chartered Accountant's certificate, total amount was received in foreign exchange directly by RTDC Ltd.

The reply of the department is not tenable as disclaimer certificate from Indian Railways was not submitted even though the Indian Railways ultimately received 56 per cent of foreign exchange earned. Further, foreign exchange earned directly by RTDC was only ₹ 906.03 lakh accordingly benefits for foreign exchange earned ₹ 2448.58 lakh by travel

agents without obtaining disclaimer certificate from them was not justified/ irregular.

- (iii) In case of other six service providers 50 duty credit scrips of ₹ 92.59 lakh were incorrectly granted on encashment of foreign currency by hotel guests at hotel counter.

RLA, Mumbai issued demand cum show cause notice to M/s Laxmi Ventures (India), while reply in respect of other scrips was awaited (January 2015).

- (iv) In case of M/s. B D & P Hotels (I) P. Ltd under RLA, Mumbai, ineligible remittance of ₹ 694.24 lakh (₹ 525.30 lakh from Saudi Arabian Airlines towards crew accommodation charges and ₹ 168.94 lakh by conversion for foreign exchange from Asian Forex Pvt. Ltd) were considered for issuing duty credit scrip without deducting the same resulting in excess allowance of duty credit of ₹ 69.42 lakh.

- (v) Five duty credit scrips amounting to ₹ 217.67 Lakh were issued by the various RLAs (Vadodara-1, Ahmedabad-1, Jaipur-1, Bangalore-1, Chennai-1) to service providers. Out of this ₹ 17.29 lakh of duty credit was issued in excess due to inclusion of FEE pertaining to different period not covered in the SFIS licences.

RLA Jaipur accepted the audit observation while, RLA Chennai issued recovery notice and recovered Rs. 4.57 lakh. RLA Bengaluru stated that the firm has not utilised the scrips fully. Further progress is awaited (January 2015).

7.20 Issue of duty credit scrips without production of prescribed documents

7.20.1 Incorrect grant of duty credit scrips of ₹60.87 lakh on time barred claims due to non-submission of document.

The last date of submission of application for SFIS is 12 months from the end of the financial year (Para 3.6 of HBP Vol. I). Delay in submission of application up to a maximum period of 2 years attract late-cut fee at the rate prescribed in Para 9.3 of HBP. Thus, claim can be filed only within a period of 2 years after expiry of due date and applications submitted after expiry of two years from due date will not be considered for entitlement .

M/s Speciality Restaurants (P) Ltd. (Mainland China) was issued 13(split) duty credit scrips (No. 210194314-26 dated 16 September 2013) for ₹60.87 lakh against FEE of ₹621.15 lakh by RLA Kolkata after late cut at the rate of two percent. On the basis of decision of the SFIS committee (meeting dated 18.07.11), the RLA called for (letter dated 22.07.11) RCMC issued by service EPC (SPEC) instead of that from FIEO. The RCMC issued on 31.08.2012 by Service EPC, New Delhi was submitted by the applicant subsequently

furnished, vide letter dated 02.09.2013. As the RCMC was submitted to RLA after a lapse of more than 2 years from last date of filing application, grant of duty credit for ₹60.87 lakh was time barred as per Para 9.3 of HBP, Vol-I.

The matter was brought to the notice of department (September 2014), their reply is awaited (January 2015).

7.20.2 An exporter applying for benefit under the FTP is required to furnish valid (on the date of application) RCMC, from the competent authority (Para 2.44 of FTP read with P.C No. 27/2007 dated 17.01.2008). Further, specific services as listed in Appendix 2 of HBP, Vol.1 are required to register themselves with SEPC. 'Hotel and tourism related services' was specifically included at Sl. No. 14 in Appendix -2 w.e.f 31.03.2008 (Public Notice No. 135 dated 31.03.2008). Thus, for availing benefit under any scheme under FTP, hotels are required to furnish RCMC from SEPC.

In case of M/s Walled City Hotel Pvt. Ltd., Jodhpur (SFIS licence No. 1310045373 dated 12.12.2013) was issued duty credit of ₹ 21.18 lakh against foreign exchange earned ₹ 211.82 lakh without obtaining/cross verification of foreign inward remittance certificate.

In six other cases at RLAs (Mumbai & Goa) duty credit scrips were issued to service providers for ₹247.23 lakh without obtaining import details.

On being pointed out in August/ July 2014, RLA Jaipur accepted the audit observation while reply of RLA Mumbai /Goa was awaited as of January 2015.

7.21 Incorrect adjustment of interest dues against duty credits through Scrips

Penalty/interest payable to Customs department is required to be paid in cash only (Para 3.17.11 of FTP).

Excess duty credit scrips were issued to M/s. Appu Hotels Ltd., (IEC No.0494016868), and other three other service providers by RLA Chennai (**Annexure 8**). These excess amounts of duty credits were later adjusted by reduction of the duty credit in the entitlements. However it was noticed that the Interest on these amounts were also adjusted along with the duty credit, instead of being recovered in cash as per the above provision.

Similarly in two cases {M/s APA Hotels (P) Ltd and M/s Hotels & Enterprises Ltd; **Annexure 9**} only the excess amount was adjusted while the interest was not recovered.

The amount of interest adjusted by adjusting the amount in amended duty credit scrips was against the provisions of FTP while ₹ 37.39 Lakh is recoverable from the beneficiaries.

7.22 Non/short levy of late cut

As per paragraph 3.6 (b) of HBP 2009-14, application for duty credit scrip shall be filed within 12 months from the end of relevant month / quarter / half-year /year. Further, as per paragraph 9.3 of HBP Vol-I, whenever application is received after expiry of due date, such application may be considered after imposition of late cut at the rate of 2/5/10 percent as applicable.

Various cases detailed in **Annexure 10** were noticed at RLAs where late cut was either not levied or short levied due to delay in submission of application for SFIS duty credit scrips. Accordingly, total late cut amounting to ₹ 61.44 lakh remains recoverable from the beneficiaries

RLA Jaipur accepted the audit observation and RLA, Mumbai issued demand notice in case of M/s Pride Hotel Ltd. RLA Puducherry intimated recovery of Rs. 0.86 lakh in case of M/s. Hi Design India Pvt. Ltd. Further progress was awaited (January 2015).

7.23 Other interesting points noticed

7.23.1 Incorrect grant of benefit under both SFIS and EPCG scheme

As per Para 5.4 (v) of EPCG scheme (FTP RE-2007), foreign exchange counted towards fulfilment of export obligation (over and above the average) shall not be eligible for incentives / rewards under promotional measures / schemes. This clause was deleted in FTP RE2008.

In case of grant of dual benefits under SFIS, and the EPCG authorizations, the DGFT issued Policy circular no. 15 (RE-2008)/2004-2009 dated 4th July 2008 and clarified that the service providers have to first utilize foreign exchange earned during 1.4.2007 till 31.3.2008 for fulfilment of pending EO under EPCG authorizations (over and above the average, if any) and SFIS would be entitled only on any additional foreign exchange earned during 1.4.2007 till 31.3.2008 thereafter. Accordingly, RLAs were directed to call for details of all pending EO under EPCG authorizations and to effect recovery in case it was found that excess SFIS benefit had already been granted for foreign exchange earned during 2007-08 in any particular case. Further, at the time of redemption of EPCG authorizations of service providers, RLAs were to ensure that SFIS had not been granted for foreign exchange earned during 1.4.2007 till 31.8.2008, which was used for discharge of pending EO against an authorization.

7.23.2 In the six cases (**Annexure 11**) FEE for the year 2007-08 were considered for export obligations under EPCG scheme as well as for SFIS claim for the subsequent years against the aforesaid provisions of Para 5.4(v) of the FTP 2009-14 introduced with effect from 19th April, 2007. Further the counting of exports for redemption under EPCG scheme in a particular year

as well as for imports made without payment of customs duty under SFIS in the subsequent year, off-set the actual exports by these beneficiaries and availing of two benefits based on the same earning This resulted in erosion of FEE defeating the intended purpose of the two schemes under FTP.

7.24 Conclusion

The hospitality sector is facilitated by the duty benefits of Foreign trade policy mainly under the two schemes; Export promotion Capital goods (EPCG) at and Served from India scheme, with the objective to earn foreign exchange.

DOC's RFD/ Strategy plans/ outcome budget does not have any specific plan for hospitality sector which contributes approximately 8-9 percent in the GDP with a total foreign exchange earnings of ₹ 2,79,749 crore during the period 2011-12 to 2013-14 with potential for further growth and employment generation. There is no single point of information on NFE earned in the hospitality sector due to the FTPs.

Audit observations covered mainly the EPCG and SFIS schemes facilitating the hospitality sector. Under the EPCG scheme, cases of incorrect / short fixation and short / non fulfillment of export obligations were noticed. Under the SFIS, cases of incorrect grant of duty credit scrips, issue of duty credit scrips to service providers having established foreign brands, non /short imposition of late cut etc. were noticed. The internal control mechanism to get assurances on the end use of the schemes in the hospitality sector has been found wanting.

Besides the above observations, several cases of lack of inter-departmental coordination, monitoring and internal control were also noticed which may lead to revenue leakages.

The department does not maintain any system manually or in the DGFT-EDI to get the assurances/ outcome about benefits availed and revenue realized by the hospitality sector which could provide feedback to the department to further refine the sectoral requirements of different FTP.