

CHAPTER V

Non- Compliance to Provisions of Various Export Promotion Schemes of Foreign Trade Policy

5.1 The Foreign Trade Policy of India (FTP) provides a framework for increasing exports of goods and services with a focus on improving trade facilitation and ease of doing business. The FTP 2015-2020 has been notified by the Central Government in exercise of powers conferred under Section 5 of the Foreign Trade (Development & Regulation), (FTDR) Act 1992, as amended. Directorate General of Foreign Trade (DGFT), under Ministry of Commerce and Industry is responsible for formulating the FTP which is implemented jointly by the DGFT and Department of Revenue.

The Export Promotion Schemes under FTP can be categorised as:

- (i) **Export from India Schemes:** These aim to provide rewards to exporters to offset infrastructural inefficiencies and associated costs involved and to provide exporters a level playing fields. The two main schemes under this category are Merchandise Exports from India Scheme (MEIS) and Service Exports from India (SEIS)
- (ii) **Duty Exemption and Remission Schemes:** These enable duty free imports or imports at concessional rates, of capital goods and other inputs for export production or duty remission to provide relief of taxes and duties suffered by the exporters in course of producing exported goods. Advance Authorisation, Duty Free Import Authorisation and Duty Drawback are important schemes under this category. The Export Promotion Capital Goods (EPCG) scheme facilitates import of capital goods under zero/ concessional rates for producing export goods and services at competitive prices.

The DGFT issues scrips to exporters under various export promotion schemes and monitors their corresponding obligations through a network of 38 regional license offices (RLAs). All 38 RLAs are computerised and connected to the DGFT Central server. To regulate imports under scrips issued by DGFT, Customs notifications are issued by CBIC and these scrips have to be registered by the exporter concerned in the Customs house under the Commissionerates. Import of inputs and capital goods under export promotion schemes are exempt, wholly or partly from Customs duties. Importers of such exempted goods undertake to fulfil prescribed export obligations (EO) as well as to comply with specified conditions, failing which the duty exempted becomes recoverable by the Customs department under the Customs Act 1962. In addition to action by

the Customs department, the licensee is liable to penal action by DGFT under FTDR Act 1992, for not fulfilling the conditions of the licence issued.

In respect of certain other schemes, under Chapter 3 of Foreign Trade Policy there is a provision of providing incentives as a certain percentage of FOB value of exports as a reward to offset the infrastructural inefficiencies and associated costs.

5.2 Persistent Irregularity regarding non-fulfilment of export obligation

Audit observations noticed during field audit are flagged through Inspection Reports (IRs) to the auditee units for their response within stipulated period of four weeks.

Over the years, audit has noticed recurring cases of **non-fulfilment of prescribed export obligations** by license holders of export promotion schemes like Advance Authorization and other schemes. As an one time exercise, all such cases noticed in compliance audit during 2000 to 2017 pertaining to 22⁴⁹ RLAs and five Commissionerates, where no action had been reported by the department, were consolidated and it was noticed that in 1043 paras, involving approx 3000 license cases issued under Advance authorisation and EPCG schemes, there was non-fulfilment of prescribed export obligation, involving revenue implication of ₹ **4205 crore** availed as exemptions and other tax benefits by the license holders.

However, neither the RLAs nor Customs Commissionerates had reported to Audit any recovery action initiated by them against the license holders for recovery of duty saved amounting to ₹ **4205 crore**, nor has the status of these cases over the entire currency of the audit period been reported to Audit.

This was pointed out to the Ministry of Commerce and Industry (October 2018) and Department of Revenue (October 2018).

Ministry of Finance, DoR accepting non-fulfilment of export obligations reported (May 2019) action in most of cases by issuing of SCNs/ demand letters/confirming of duty demand and initiation of recovery action. In some cases DoR reported that Customs did not have details about the registration of authorization and have called licence details from DGFT. However, the DoR not accepting audit comments about pursuing the defaulter cases reported that

⁴⁹ RLAs: Vadodara, Ahmedabad, Rajkot, Bengaluru, Panipat, Amritsar, Chennai, Trichy, Coimbatore, Puducherry, Madurai, Hyderabad, Vishakhapatnam, Cuttack, Kolkata, Varanasi, Moradabad, Dehradun, Kanpur, Mumbai, Surat and Pune. Commissionerates: Sikka, ICD Bengaluru, ACC Bengaluru, Chennai Sea and Customs (P) Nautanvas

instructions/circulars have been issued (January 2011/ October 2016) to field formations for monitoring of performance.

The fact remains that despite issue of instructions, Customs field formations have not initiated the recovery action after expiry of three months from EO period as prescribed in the import notifications for which the license holders have furnished Bond/Security/Surety to the Custom authorities.

Ministry of Commerce and Industries, accepted non fulfilment of EO in 219 cases and stated that show cause/demand notices have been issued. In another 215 cases, Ministry stated that Export Obligation Discharge Certificates (EODC) were already issued to the importers on fulfilment of EO. However, details of EODCs were not provided to audit for verification. Ministry stated that 148 cases were under examination. In remaining cases, Ministry's reply is awaited (October 2019).

5.3 Deficiencies in fulfilment of export obligation under Export Promotion Capital Goods (EPCG) scheme

In order to encourage exports in the manufacturing sector, the Foreign Trade Policy, under the Export Promotion Capital Goods (EPCG) scheme, allows import of capital goods at zero or concessional rates of duty. In turn, the scheme imposes an export obligation (EO) on the exporters/manufactures availing this scheme, to export goods manufactured out of imported capital goods, to the extent of six/eight times⁵⁰ of import duties saved on capital goods imports. The export obligation is to be fulfilled over a period of six/eight years⁵¹ from the date of issue of authorisation. Concessions allowed on duties on such imports constitute revenue foregone, which would have otherwise accrued to the Government. In the event of default in fulfilment of EO, the licence holder is to pay back duties in proportion to the unfulfilled amount of EO along with specified interest.

DGFT issues conditional licences to be registered with specific Customs port along with execution of bond and bank guarantee as prescribed. DGFT and Customs departments are responsible for implementation and monitoring of the Scheme. The total revenue foregone on export promotion schemes by way of concessional duties and incentives during FY 2017-18 was ₹ 41,477 crore. The EPCG scheme, together with three other major export promotion schemes accounted for 91 per cent (₹ 38,010 crore) of total revenue foregone. The issue of non-fulfilment of EOs along with several systemic deficiencies by EPCG scheme licence holders were pointed out in an earlier performance audit

⁵⁰ Export obligation is six times in case of imports at zero duty and eight times of duty saved in case of concessional 3% duty

⁵¹ For zero duty and 3 % concessional rate , respectively

reported in 2011 (AR No. 22 of 2011). The CAG had recommended, inter alia, strengthening of monitoring coordination and monitoring mechanisms of the departments concerned, namely, the DGFT and Customs, which was accepted by the Government. Deficiencies in the implementation of EPCG scheme have been regularly noticed during transactions audit of the EPCG licenses, which has already been pointed out to the ministry as reported under para 5.2 of this report.

Audit carried out a review of EPCG licenses due for redemption during 2017-18 based on a sample of files selected from three RLAs⁵², an issue which has been recurrently commented upon in the audit reports. The findings of the EPCG licences review are reported in the long paragraph below.

5.3.1 During 2008-09, 19931 EPCG licences were issued with CIF value of ₹17,037 crore and obligation to export products worth ₹1,38,440 crore. RLAs Mumbai, Goa and Pune accounted for 22 per cent of licences issued during 2008-09.

Accordingly, sample of licences issued by following three RLAs under Western Zone was examined:-

- (i) Additional DGFT, Mumbai,
- (ii) Joint DGFT, Pune and
- (iii) Deputy DGFT, Goa

Audit selected a sample of 688 licences issued during 2008-09 which were due for redemption as on 31 March 2017. A few licences issued in the earlier period but still pending for redemption were also selected. Out of 688 licence cases requested by audit, 626 case files were made available for audit as shown in the table below:

Table No. 5.1

Sl. No.	RLA	FY	Licences issued	Duty credit (Cr. ₹)	No. selected	No. furnished and audited	Duty credit (Cr. ₹)
1	Addl. DGFT, Mumbai	2008-09	3042	5205	444	404	2224
2.	Jt.DGFT, Pune	2008-09	857	542	176	157	348
3.	Dy.DGFT, Goa	2005-06 to 2008-09	567	160	68	65	72
			4466	5907	688	626	2644

⁵² Additional DGFT, Mumbai, Joint DGFT, Pune and Deputy DGFT, Goa

Audit findings

5.3.2 Inaction by the department to recover duty benefits availed despite non-fulfillment of export obligation by licence holders

As per para 5.2 of FTP, import of capital goods at 3 percent rate of duty was allowed subject to achievement of EO equivalent to eight times of duty saved on import of capital goods to be achieved block wise in eight years from date of issue of licence. The licence holder is required to fulfill EO upto 50 per cent in the block of 1 to 6 years and balance 50 per cent in the block of 7 to 8 years. It is compulsory on the part of licence holder to submit to RLA concerned by 30th April of every year, a progress report on block-wise fulfillment of EO. On completion of EO period of eight years the licensee is required to submit evidence regarding completion of prescribed EO for redemption of the licence. The importer within 30 days from the expiry of each block from the date of issue of licence produces evidence to Customs authorities showing the extent of EO fulfilled.

Further, authorization holder shall produce, within six months from date of completion of import, to the concerned RLA, a certificate from the jurisdictional Customs authority or an independent Chartered Engineer, at the option of the authorisation holder, confirming installation of capital goods.

The importer executes a bond/surety/security to Customs authority binding himself to fulfill conditions of the licence which includes installing the imported capital goods and fulfillment of prescribed EO. If the export obligation or conditions of the licence are not fulfilled, the importer shall within three months from the expiry of the said block pay duties together with interest.

Audit noticed from the examination of the licence files that the department had not issued demand notices in 173 cases even though EO period had expired. Further, the department had not issued SCNs where importers did not respond to demand notices in 60 cases in contravention to the prescribed procedure. A few cases are illustrated below:

- i. **EPCG for export of wind turbine generator** : RLA, Mumbai had issued two EPCG licences to an importer during the FYs 2007-08 and 2008-09 with duty saved amount of ₹ 47.45 lakh and ₹ 1.26 crore respectively. The EO period has ended in March and May 2016 and three months' time to file statement of exports has also ended. On examination of licence files it was noticed that the licence holder had imported capital goods at concessional rate of duty to manufacture export goods i.e wind turbine generator and related equipment. However, there was no evidence available in the files regarding compliance by the importer to any conditions of the licence, viz, submission of installation certificates within six months from date of completion of imports, annual report on EO fulfilment, block wise achievement of EO etc.

Audit did not find any evidence that the department had initiated penal any action or co-ordinated with Customs department for reporting non-fulfilment of prescribed EO.

Further verification in EDI system of RLA, Mumbai revealed that the department had issued another 28 licences to the importer during the period April 2008/February 2009 involving duty saved amount of ₹ 6.12 crore. In all these licences the importer had not submitted installation certificates and other performance documents, despite which no action from the department was observed to have been initiated in DGFT EDI system.

On this being pointed out (February 2018), the RLA issued (April 2018) notices to the licence holder. Response from DGFT, New Delhi is awaited (October 2019).

Department of Revenue (DoR), CBIC reported (July 2019) that in 14 cases SCN/demands have been confirmed and in remaining 16 cases Customs did not have registration details of authorisations, which have been sought from DGFT.

- ii. **EPCG for import capital goods for export of Smart cards and accessories** : RLA, Pune had issued one EPCG authorisations to an importer during FY 2008-09 with duty saved amount of ₹ 1.10 crore to exports goods e.g. smart cards and accessories worth ₹ 8.86 crore within a period of eight years. Examination of the records revealed that although the importer had not complied with the conditions of licence i.e. furnishing installation certificate, furnishing block wise achievement of EO, Annual performance reports and the department has not taken penal action on the defaulter nor had informed the Customs department.

From the DGFT EDI system it has been noticed that another 7 licences were issued by RLA, Pune during FYs 2006-07 to 2008-09 involving duty saving of ₹ 6.99 crore. Scrutiny of the records revealed that in these cases also the importer had not complied with the conditions of licence i.e. furnishing installation certificate, furnishing block wise achievement of EO, Annual performance reports and the department has not taken action on the defaulter.

On this being pointed out (July 2017), the RLA intimated (July 2017) issue of demand cum SCN.

- iii. **Export Obligation not met through retail counter sales:** RLA, Mumbai had issued fourteen licences to an importer during the period 2007-08 and 2008-09 involving duty concessions of ₹ 10.73 crore with export obligation of ₹ 85.80 crore. Test check revealed that the license holder had imported

goods like fixtures, glazed tiles, HDMI splitters, cables etc., at concessional rate of duties and EO was proposed to be met by retail counter sales in foreign currency. However during the entire period of eight years the importer did not comply with any of the conditions of licences. No action was taken by the department, though the EO period expired in all fourteen licences (2016-17).

On this being pointed out, the RLA had issued demand notice on 16 March 2018, to which importer stated that they are in the process of filing a representation to the EPCG Committee, New Delhi, to get reduction in export obligation .

It is obvious that importer did not comply with the conditions during the entire period of eight years, and only on receipt of notice which was issued after audit intervention, had tried to approach EPCG committee for relief in EO.

- iv. **Export Obligation not met for hotel and tourism services** : A license holder engaged in running a five star hotel had been issued eight licences during FY 2008-09 by RLA, Pune with duty saved amount of ₹ 4.08 crore. The statement of year wise EO fulfilment revealed only 20 per cent to 35 per cent of export obligation has been fulfilled in eight licences. The RLA had not initiated any action for non-fulfilment of block wise EO, though the period of all licences expired by March 2017 and no extension was sought before expiry of EO period. The proportionate duty recoverable was ₹ 2.59 crore.
- v. **Import of Mercedes Benz under EPCG**: A hotel and tourism service provider was issued a licence (January 2007) by RLA, Goa to import Mercedes Benz car for its hotel industry. However the basic condition that vehicle was to be registered as Tourist vehicle was not met so far. The SCN was issued after a delay of seven years but could not be served to the licence holder as the hotel had closed by that time. The department had not explored other ways or coordinated with Customs department to find out the licence holder and to recover the concessional duty of ₹ 24.53 lakh extended to the licensee.
- vi. **Export obligation of a jewellery unit met through ineligible exports from EOU** : In fourteen licences issued by RLA, Mumbai to a jewellery unit with duty saved amount of ₹ 1.98 crore, the importer had furnished export performance in 12 licences, to which department issued deficiency letters between October 2012 and March 2016 as the licensee had included ineligible exports i.e. exports from EOU units in export performance.

However, licensee did not respond to the deficiency letters of the RLA, but the department had not taken any further action by issuing SCNs.

In the test checked cases, Audit noticed that RLAs had either failed to issue cautionary letters or to initiate any other pre-emptive action to recover duty when the conditions of the licence were not met as prescribed in para 5.17 of HBP vol.1. Audit did not find evidence that RLAs had any mechanism to keep track of receipt of installation certifications, year wise export performance reports, and follow-up mechanism to track block wise default in meeting the EO. DGFT EDI system was also not enabled to get licence wise performance from the Customs department on regular basis or any alert about non-achievement of block wise EO. DGFT authorities still depend on manual submission of evidence to redeem licences under the Scheme.

On this being pointed out (July 2017 to March 2018), concerned RLAs reported (July/April 2018) issue of demand notices or SCNs in 165 cases involving duty of ₹ 219.73 crore. Reply from DGFT is awaited (October 2019)

5.3.3 Redemption of authorization by considering ineligible foreign exchange earnings

Vide paragraph 5.3 & 5.5 of the FTP, EPCG scheme is also extended to service providers like hotel and Restaurant (including catering) industry where EO is to be fulfilled by foreign exchange earnings out of hotel and restaurant services rendered to foreign visitors. As per paragraph 9.5.3 (ii) of FTP, 'Service provider' includes a person providing supply of a service from India to service consumer of any other country in India. Foreign exchange earned out of authorized services⁵³ shall only be counted towards EO. Forex earned out of mere currency exchange services are not be counted towards EO.

RLA, Pune had allowed redemption of fourteen EPCG licences issued to two license holders who were engaged in hotel and restaurant industry in Pune. The EO was met from foreign exchange earned out of international card payments of foreign visitors and partly through forex earned in cash of ₹ 2.51 crore for unspecified services, not supported with service bills. Counting amount of ₹ 2.51 crore towards EO fulfillment was not in order.

On this being pointed out (August 2017), RLA, Pune stated (January 2018) that the license holders had submitted additional Foreign Inward Remittance Certificates (FIRCs) for ₹ 2.51 crore and regularized the redemptions.

RLA, Pune while regularizing the redemption on receipt of additional FIRC failed to impose any penalty for incorrect fulfillment of EO in the earlier instance.

⁵³ Hotel and restaurant services

The fact remains that the licence was incorrectly redeemed, and it was only after Audit pointed out the irregularity the FIRC's were called for by the department indicating that that no due diligence was made even at the time of redemption of licence.

5.3.4 Redemption of licenses on the basis of incorrect consideration of average exports

Export Obligation under EPCG scheme is required to be fulfilled by export of goods manufactured/services rendered by the applicant. There are two types of export obligation. Average export obligation (AEO) in which export obligation is over and above, the average level of exports achieved by the authorization holder in the preceding three licensing years for the same and similar products within the overall export obligation period. Such average would be the arithmetic mean of export performance in the last three years for the same and similar products. Specific export obligation is 8 times the duty saved amount in which the Authorization holder shall also fulfil a minimum of 50 per cent export obligation in each block of years-the first block being of 6 years and the second block is of 2 years.

In terms of paragraph 5.5 of FTP 2009-14 specific EO fixed for a licence under the scheme shall be over and above the average level of exports achieved in the preceding three years for the same and similar products. The licence holder has to achieve specific EO separately, while maintaining average level of exports in each year during which specific EO was achieved.

Policy Interpretation Committee of DGFT vide their meeting No.5/AM12 dated 9 September 2011 had reiterated that Average export obligation (AEO) shall be fixed by taking into account the average of same and similar exports of last three years. If the unit is in existence for less than three years, the AEO shall be the average of exports of years during which unit existed.

Following cases were noticed in which the RA had incorrectly considered average exports and had redeemed the licences:

- (i) RLA, Mumbai had redeemed the licence issued to an importer accepting the achievement of specific EO and AEO maintained during FYs 2010-11 and 2011-12. Verification of list of shipping bills furnished for specific EO and AEO indicates that 19 shipping bills involving FOB value of ₹ 15.13 crore were double counted for both EO and AEO. This resulted in shortfall in the net specific EO by ₹ 13.68 crore, and incorrect redemption of licence without checking the double use of shipping bills.

On this being pointed out (May 2017) the department stated (March 2018) that the exporter had deleted 19 shipping bills from list of AEO, and still AEO maintained was more than required AEO of ₹ 1126.41

crore (F.No.03/97/021/00940/AM09 dated 6 March 2018, Additional Director General of Foreign Trade, Mumbai).

The reply is not acceptable because the department has addressed the issues only after audit pointed the irregularity. Further, reasons for inclusion of these 19 shipping bills twice despite provisions to the contrary were not addressed.

- (ii) RLA, Mumbai issued (July 2008) EPCG licence to an importer in textile industry and imposed the AEO considering the unit existed for three years. However, verification by audit revealed that unit was in existence for two years FY 2006-07 and 2007-08, AEO shall be the average of two years instead of three years, resulting in short fixation of AEO by ₹ 15.63 lakh. The licence was redeemed on 1 November 2016 on the basis of incorrect AEO.

On this being pointed out the RLA re-fixed the AEO at ₹ 46.87 lakh which the firm had maintained.

The fact remains that issue of licences and fixation of EO requires comprehensive scrutiny by RA to avoid such instances.

5.3.5 Incorrect fixation of export obligation

EPCG licences are issued subject to achievement of EO equivalent to eight times of duty saved in eight years. However in case of Small Scale Industry (SSI) units, the EO is fixed at lower rate, equivalent to six times of duty saved on capital goods imported, provided the CIF value of such imported does not exceed ₹ 50 lakh and total investment in Plant & Machinery after such imports does not exceed SSI limit. If the CIF value of import exceeds ₹ 50 lakh, EO was to be fixed at 8 times instead of 6 times of duty saved.

RLA, Pune had issued authorisation dated 12 May 2008 to an importer with duty saved amount of ₹ 69.01 lakh and EO of ₹ 4.14 crore (6 times of duty saved) to be achieved in eight years. Since the import sought through authorization was in excess of the limit of ₹ 50 lakh, the benefit of SSI unit ie 6 times of duty saved should not have been extended to the importer. This resulted in short fixation of EO by two times amounting to ₹ 1.38 crore.

On this being pointed out, RLA intimated issue of a demand cum SCN (September 2017). Further progress is awaited (October 2019). DoR stated that that the paragraphs pertain to DGFT.

Overall audit's test check revealed that duty benefits of ₹ 306 crore had been availed by the licence holders without meeting the conditions of EPCG. Issues like non fulfillment of export obligation, irregular issue of EPCG licences, delayed action being taken on defaulters, incorrect fixation of export obligation and irregular redemption of authorizations continued to plague the scheme in large number of cases.

Ministry of Finance, DoR accepted non-fulfilment of export obligations and reported (May 2019) that action in 206 cases has been taken by way of issuing of SCNs/ demand letters/confirming of duty demand and initiation of recovery action. In 40 cases, DoR reported that Customs did not have details about the registration of authorization and have called licence details from DGFT. DGFT's response was awaited (October 2019).

Ministry's response reaffirmed the audit's observation regarding non-fulfilment of export obligation pursuant to benefits availed under the EPCG scheme is a persistent problem thus nullifying the impact of duty benefits allowed for export promotion to the extent that export obligations remain unfulfilled. Further, Ministry's response regarding cases where details of registration of authorization were not available with them indicated weak monitoring and information exchange mechanisms between the Customs and DGFT authorities, as each EPCG license authorised by the DGFT is to be registered with Customs authorities before imports could be effected under these licenses.

DoR not accepting audit comments about weak information exchange mechanism to pursue the defaulter cases reported that Customs EDI system is sharing Shipping bill data with DGFT on regular basis for exports made under EPCG scheme. In so far monitoring and co-ordination by CBIC field formations with DGFT were concerned, instructions/circulars had been issued (January 2011/ April 2015/October 2016/May 2017) to field formations for setting up of institutional mechanism for exchange of information with RLAs and holding a quarterly meeting to pursue EO fulfilment status where period has expired.

Ministry's response did not support the ground reality which showed that despite issue of instructions and setting up of institutional mechanism for pursuing EO fulfilment cases, Customs field formations had not suo moto initiated the recovery action after expiry of three months from EO period as prescribed. Action for recoveries was initiated only in cases test checked when pointed by Audit.

5.4 Non-compliance to provisions of Other Export Promotion Schemes

During test check of records pertaining to transactions between (July 2014 to February 2017), Audit noticed irregularities regarding short levy of duty on Domestic Tariff Area (DTA) clearances, non-achievement of minimum value addition, non-recovery of drawback where exports proceeds have not been realized, Non/short imposition of late cut, grant of excess credit and grant of duty credit on time barred claims.

Total revenue implication involved in these 39 cases was ₹ 40.51 crore where duty exemptions were availed of without fulfilling Foreign Trade Policy (FTP)

or Hand Book of Procedures (HBP) provisions. Out of these, seven cases are discussed in the following paragraphs and 32 cases involving revenue ₹ 19.04 crore which have been accepted by the department and recoveries made/ recovery proceedings initiated are mentioned in **Annexure 11**.

Export Oriented Units (EOUs)

5.4.1 Clearance of restricted goods in DTA

As per paragraph 6.8 (h) of Foreign Trade policy (FTP) 2009-14, Export Oriented Unit (EOU) may sell products in domestic tariff area (DTA) which are freely importable⁵⁴ under FTP, under intimation to the Development Commissioner and against payment of full duties, provided they have achieved positive NFE. No DTA sale is permissible in case of pepper and pepper products and marble. Further, as per DGFT notification no.38-RE/2013 dated 26 August 2013, 'Granite' (ITCH Code 68029300) are freely importable if the c.i.f.⁵⁵value per square meter is USD 80 and above.

An EOU under Kutch Commissionerate (Central Excise and CGST) had cleared 12949 square meter of 'Granite slab and tiles' valuing ₹ 7.59 crore in DTA during 2014-15 and 2015-16. Audit scrutiny revealed that granite slabs cleared in DTA were having value of USD 39.96 and USD 34.14 per sqm for the year 2014-15 and 2015-16 respectively, which was lower than USD 80 per square meter prescribed by aforesaid DGFT notification, hence they did not qualify as freely importable products. This resulted in irregular clearance of 12949 square meter of restricted goods granite slab and tiles valuing ₹ 7.59 crore in DTA Area.

On this being pointed out, Ministry of Finance, Department of Revenue reported (January 2019) that a show cause notice issued in January 2019 is under adjudication. Further progress is awaited (October 2019).

Incentive and Reward Schemes (IEIS)

5.4.2 Lack of provision to recover benefits given under on re-import of exported goods

In terms of notification no.94/1996-cus dated 16 December 1996, duty free re-import of export goods is permissible subject to following conditions:

- i. If the goods were exported under claim of drawback of customs and excise duties levied by the Union, the amount of drawback of customs and excise duties are repaid.

⁵⁴ Items are freely importable when no 'Authorisation' or permission is required for being imported into the country or exported out.

⁵⁵ CIF- Cost, Insurance and freight

ii. If the exported goods were under the claim of rebate of excise duty or under bond without payment of excise duty, the amount of excise duty is paid.

iii. If the exported goods were under Duty exemption pass book (DEPB) scheme, the amount of excise duty leviable on importation plus the amount of drawback allowed at the time of export subject to condition that the importer produce the DEPB scrip before the proper officer for debit of the amount equal to the amount of DEPB credit permitted on the exported goods which is being imported.

In the case of shipping bills for goods exported under duty drawback scheme, in addition to drawback paid by customs department, the Director General of Foreign Trade (DGFT) grants duty credit scrips under incentive and reward schemes under chapter 3 of the FTP, which are utilized for paying customs duty on import of goods. If goods exported under drawback scheme are re-imported under notification no.94-1996-cus dated 16 December 1996, there is provision in the notification for recovery of drawback involved in the re-imported goods. But there is no provision in the notification for recovery of duty credit granted by DGFT under incentive and reward schemes.

Audit scrutiny of the bills of entry for goods re-imported under notification no.94-1996-cus dated 16 December 1996 through Chennai Sea Customs, Chennai Air Customs, Tuticorin Sea Customs and ICD St. Johns, Tuticorin for the period 2012 to March 2013 revealed that wherever goods exported under duty drawback scheme were re-imported, only the duty drawback paid to the exporter had been recovered. Duty credit granted under reward and incentive schemes under chapter 3 of the FTP was not recovered. Cross verification of shipping bills of re-imported goods with the DGFT EDI data in test checked cases revealed that in 376 cases of re-import, RLA, Chennai had granted duty credit benefits of ₹ 1.25 crore under chapter 3 of FTP, which could not be recovered in the absence of provision in aforesaid notification.

The matter was communicated to the concerned customs Commissioners in June 2017. Tuticorin Customs, Commissionerate, while accepting that there was no provision to recover the duty credit under reward and incentive scheme under chapter 3 of FTP, however, reported recovery of such credit availed along with interest in respect of two importers which amounted to ₹ 0.73 lakh (March 2018). Chennai Air Customs in their reply had stated (March 2018) that demand notices have been issued to the firms. Reply in respect of other Commissionerates is awaited (October 2019).

5.4.3 Incorrect grant of benefit to ineligible exporter

According to paragraph 3.14.5 of FTP. 2009-14, inserted vide notification no.3 (RE-2013)/2009-14 dated 18 April 2013, Incremental exports incentivisation schemes (IEIS) on annual basis was introduced with the objective to incentivize incremental exports. Under the scheme, an IEC holder was entitled for a duty credit scrip at the rate of two per cent of the incremental growth in terms of FOB value of exports (achieved by the IEC holder) during the current year (say 2013-14) compared to the exports made in previous year (say 2012-13). Exports which are subject to minimum export price or export duty are ineligible for grant of IEIS benefits (vide notification no.43 (RE-2013)/2009-14 dated 25 September 2013).

Additional Director General of Foreign Trade (ADGFT), Kolkata issued (January 2015) a duty credit scrip for ₹ 36.37 lakh to an importer under IEIS for incremental growth in the financial year 2013-2014 (57 SBs) vis a vis financial year 2012-13 (5 SBs). However, scrutiny of five shipping bills pertaining to year 2012-13 revealed that all the bills pertained to export of de-oiled rice bran to Bangladesh and in all cases export duty was paid. This rendered the exporter with no eligible exports in 2012-13 and consequently ineligible for grant of benefit under IEIS for the year 2013-14. Thus, the duty credit granted in this case amounting to ₹ 36.37 lakh was incorrect/ineligible.

This was pointed out to the Ministry in September 2018, their reply is awaited (October 2019).

Served from India Scheme (SFIS)

5.4.4 Grant of excess credit due to non-deduction of tax involved

According to paragraph 3.12.2 and 3.12.4 of FTP 2009-14, Indian service providers of services listed in Appendix 41 of Handbook of Procedure (HBP) Vol-I (2009-14) would be eligible for SFIS scrip on net foreign exchange earned. Paragraph 3.6.1 of HBP, Vol-I (2009-14) provides that foreign exchange remittances other than those earned for rendering of services would not be counted for entitlement. Further, DGFT trade notice no.11/2015-20 dated 21 July 2016 has clarified that State/Central taxes payable to Governments collected by the services provider from the customer are not earnings of service provider and hence entitlement shall be regulated accordingly.

Audit scrutiny of SFIS scrips issued by JDGFT, Cochin and JDGFT, Thiruvananthapuram to service providers engaged in hotel and tourism related services revealed that, while sanctioning SFIS credit scrips, taxes included in the gross remuneration received for services, namely Service tax (12.36 per cent), Luxury tax (12.5 per cent) and VAT of food (14.5 per cent) collected by the

service provider were not deducted from the gross foreign exchange earnings. This resulted in grant of total excess credit of ₹ 60.80 lakh by both JDGFT offices at Cochin (four licencees) and Thiruvananthapuram (six licencees).

On this being pointed out, DFGT, New Delhi reported (August 2018/March 2019) recovery of ₹ 33.49 lakh including interest from service providers. The name of one service provider was put under Denied Entry List (DEL), while one service provider surrendered two scrips valued ₹ 9.93 lakh under protest and filed a writ petition in High Court of Kerala. Further progress is awaited (October 2019).

5.4.5 Other irregularities:

5.4.5.1 Incorrect discharge of obligation

Paragraph 5.7 of Foreign Trade Policy (FTP) 2009-14, stipulates that in case of direct imports, export obligation shall be reckoned with reference to actual duty saved amount, whereas in case of domestic sourcing of capital goods, export obligation shall be reckoned with reference to notional customs duties saved on Free on road (FOR)⁵⁶ value.

In 20 EPCG authorization issued to four importers where RLA, Ahmedabad issued export obligation discharge Certificate (EODC), audit observed that in 17 authorizations, applicants invalidated the authorization as direct imports though the capital goods were sourced indigenously. On scrutiny of the documents, it was noticed that RLA allowed discharge of their export obligation against licencees allowing domestic procurement after treating duty saved amount on account of central excise duty instead of notional customs duty as required under paragraph 5.7 of FTP *ibid*. This had resulted in short fulfilment of export obligation at ₹ 11.38 crore.

On this being pointed out DGFT, New Delhi stated (June 2018) that in one case revised papers submitted for re-fixation of EO are being examined. In remaining three cases the firms have been asked to show fulfilment of revised EO. In case of non-compliance, action under FTDR Act would be taken. Further progress is awaited (October 2019).

⁵⁶ FOR is Freight on road also known as Free on road. The cost incurred in transporting goods from the supplier to the client without any transportation charges to the purchaser/client.

5.4.5.2 Non/short imposition of late cut

Paragraph 3.6 (b) of Handbook of Procedures (HBP), 2009-14 stipulates that application for duty credit scrip shall be filled within 12 months from the end of relevant month/quarter/half year/year. Further, as per paragraph 9.3 of HBP, 2009-14, 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 per cent as applicable.

Out of 864 licences with total value of ₹ 46.11 crore of Focus Market Scheme (FMS), VKGUY, Served from India Scheme, Incremental Export Incentivisation Scheme and Focus Product Scheme issued by Joint Director of Foreign Trade, Jaipur during 2016-17, Audit test checked 107 licences with value of ₹ 6.71 crore and observed that in 23 applications (28 licencees) for duty credit scrips under aforesaid schemes were filed after the prescribed date of submission but the credit scrips were issued/granted without/short imposition of late cuts. Further, in five cases the credit scrips under FPS/FMS were issued/granted on the time barred shipping bills. This has resulted into non/short imposition of late cut amounting to ₹ 20.65 lakh on total duty credit scrips issued for ₹ 1.96 crore.

On this being pointed out, the DGFT admitting the observations reported (September 2018) recovery of ₹ 20.65 lakh from 26 licencees, issued SCN to M/s A Exports and placed M/s B Trading Company, under Denied Entity List (DEL). Further progress is awaited (October 2019).

5.4.5.3 Irregular grant of duty credit on time barred claims

As per paragraph 3.11.9 of Handbook of Procedure (HBP), 2009-14, application for obtaining duty credit scrip under chapter 3 of FTP shall be filed within a period of twelve months from the date of export or within six months from the date of realization or three months from the date of printing/release of shipping bill, whichever is later. Further, as per paragraph 9.3 of HBP 2009-14, any application, received after expiry of last date, the application may be considered after imposing a late cut at the rate of 2 per cent, 5 per cent and 10 per cent for application received after the expiry of last date but within six months, application received after six months date but not later than one year and application received after 12 months but not later than 2 year respectively.

Three exporters were issued (May to November 2014) duty credit scrips of ₹ 25.53 lakh under VKGUY, FPS and FMS schemes under chapter 3 of FTP by RLA Ahmedabad after imposition of late cut (10 per cent) though applications have been submitted after expiry of three years from the date of exports and two and half years from the date of realization prescribed under aforesaid

paragraph 3.11.9 read with 9.3 of HBP 2009-14. This resulted in irregular grant of duty credit of ₹ 25.53 lakh on time barred claims.

On this being pointed, DGFT, New Delhi while accepting the observation reported (November 2018/July 2019) that the firms paid duty plus interest amounting to ₹ 30.62 lakh.

5.5 Conclusion

Persistent non-fulfilment of export obligation, as pointed out by audit, clearly indicated that the system to ensure that benefits availed by the exporters matched with required export performance were closely monitored, was absent in the DGFT. Government may review all the cases of non-fulfilment of export obligation besides those pointed out in audit, and take steps to strengthen the monitoring mechanism both through their IT platforms and through plugging weaknesses in implementation of the prescribed rules and procedures.

The test audit of 37 Regional licensing authorities revealed instances of violations of prescribed rules and procedures framed to give effect to the provisions of the Foreign Trade Policy and Procedures regarding fulfilment of export obligations and awarding export incentives. The cases pointed out in above paragraphs are illustrative based on audit's test check and similar violation of rules and procedures and errors of omission and commission by the officers responsible for issue and discharge of licenses cannot be ruled out. Department is advised to review all cases of non-fulfilment of conditions EPCG and other schemes.