

**PROFESSIONAL PROGRAMME
STUDY MATERIAL**

**ADVANCED TAX
LAWS AND
PRACTICE**

MODULE III - PAPER 6



**THE INSTITUTE OF
Company Secretaries of India**

IN PURSUIT OF PROFESSIONAL EXCELLENCE
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PROFESSIONAL PROGRAMME

ADVANCED TAX LAWS AND PRACTICE

This Study Material is designed for the benefit of the students preparing for the above subject under the Professional Programme and written in lucid and simple language for the benefit of the students.

The course material is unique in its treatment of various provisions of the relevant Acts. Income Tax, Central Excise and Customs pose the peculiar problem of being subjected to frequent changes either by legislative amendments or by issue of notifications, orders, trade notices etc. Every effort has been made to give the latest information, wherever possible including changes made by the Finance Act, 2012.

While writing the study material an attempt has been made to present the material in a unified and cohesive manner, giving the blend of provisions of tax laws and tax practices. All the important areas of tax planning connected with the foresight of tax management included in the various study lessons, call for analytical application by the students and require thorough knowledge of the provisions of tax and case laws.

Further, the incidence of tax planning is so crucial to the managerial decision-making process that it becomes important to keep oneself abreast of the innovations/developments taking place in these areas. Therefore, students are expected to regularly update themselves by a systematic and regular reading of the current literature on the subject, like leading journals and financial dailies in addition to various circulars and notifications, etc. issued from time to time by the CBDT and CBEC.

This paper comprises three parts. The first part (Part A) deals with 'Direct taxation' the second part (Part B) deals with the 'Indirect taxation' and the third part (Part C) deals with the 'International Taxation'.

The 'Direct Taxation' part includes, general framework of direct taxation in India, corporate taxation, tax planning and tax management. Corporate tax issues are adequately covered with emphasis on tax planning and other relevant issues. Tax management is not merely a legal exercise attempted in isolation, but a method of integrating all areas of management. Almost every financial decision in the company has tax implications. The corporate bodies are expected to maintain integrity of the industry by adopting the line of tax planning which is permissible within the framework of tax laws, thus bringing in its fold the healthy practices of tax morality in the national interest and in their own interest.

The 'Indirect taxation' (Part B of study material) includes, Central Excise laws, Custom laws, Promissory Estoppel in Fiscal laws and tax planning and management. Indirect Taxes on the other hand have assumed enormous significance now. Speaking of excise duties, it has a wide coverage involving every manufacturing activity attracts excise duty levy whether the activity is carried on in – small scale, medium scale or large scale. It has assumed the role of a line function mainly in the

corporate sector, in view of not only cash flow implications but also profit planning. But, a sound knowledge of procedural and substantive provisions of these indirect tax laws is a sine quo non for a proper direction to overall corporate planning.

'International Taxation' aspect of the study material (Part C) is a thorough self contained work covering entire gamut of this dynamic concept. Much stress and emphasis given to the modern practices followed abroad and interplay with domestic statutory laws.

The 'International Taxation' part includes basic concepts governing international taxation, Advance Rulings, taxation of inbound transactions and taxation of outbound transactions. International taxation is new induction in the Study Material for taxation. The Study material incorporated relevant information and issues relating to International Taxation but there is avenue for further improvement. Since the topic is new and dynamic, emerging developments has been given due credence.

Students, however, should endeavour to refer to the suggested readings in each study lesson to keep themselves up-to-date. In the event of any doubt, students may write to the Directorate of Academics and Professional Development in the Institute for clarification. Students are also advised to meticulously go through 'Student Company Secretary' and 'Chartered Secretary' journals of the Institute.

The Company Secretary being well trained in interpreting statutes and ensuring compliance with procedural requirements is best suited to handle indirect taxation matters, particularly when there is no positive evidence of other professionals having made any serious and consistent efforts to enter this area. Besides, indirect taxes have a tremendous scope for a fulfilling practice, for a Practising Company Secretary.

Each study lesson has been devised with a view to making it a self-contained note on the topic covering the substantive as well as procedural aspects. The size of each study lesson is such as to conduce to a graduated approach to understanding indirect taxes. In view of the comparatively complex nature of the paper, the division of study lessons has been made in such a way as to facilitate easy understanding.

Although care has been taken in publishing this study material yet the possibility of errors, omissions and/or discrepancies cannot be ruled out. This publication is released with an understanding that the Institute shall not be responsible for any errors, omissions and/or discrepancies or any action taken in that behalf.

Should there be any discrepancy, error or omission noted in the study material, the Institute shall be obliged if the same are brought to its notice for issue of corrigendum in the Student Company Secretary.

The students may note that this study material is updated upto the Finance Act, 2012 and will be applicable for June 2013 and December 2013 examination.

(v)

PROFESSIONAL PROGRAMME
SYLLABUS
FOR
ADVANCED TAX LAWS AND PRACTICE

Level of knowledge : Expert knowledge

Objectives :

To provide —

- (i) knowledge of framework of taxation system in India.
- (ii) knowledge of various concepts and their application relating to tax laws with a view to integrating the relevance of these laws with financial planning and management decisions.
- (iii) an overview of international taxation.

***Detailed contents* :**

PART-A : DIRECT TAXATION - LAW AND PRACTICE (30 MARKS)

1. General Framework of Direct Taxation in India

Different direct tax laws and their inter-relationship; importance of Income Tax Act and Annual Finance Act and related Constitutional provisions; harmonisation of tax regime.

2. Companies under Income-tax Laws

Classification and tax incidence; corporation tax as per Article 366; computation of taxable income and assessment of tax liability considering special provisions relating to companies.

3. Tax Planning

Concept of tax planning; Tax planning with reference to setting up a new business; locational aspects; nature of business; tax holiday, etc.

Tax planning with regard to specific management decisions such as mergers and takeovers; location of undertaking; introduction of voluntary retirement; tax planning with reference to financial management decisions such as borrowing or investment decisions; reorganisation or restructuring of capital decisions.

Tax planning with respect to corporate reorganization; tax planning with reference to employees' remuneration.

Tax planning vis-à-vis important provisions of wealth-tax including court rulings and legislative amendments.

4. Tax Management

Return and procedure for assessment; special procedure for assessment of search cases, e-commerce transactions, liability in special cases; collection and

(vi)

recovery of tax; refunds, appeals and revisions; penalties imposable, offences and prosecution.

PART-B : INDIRECT TAXATION – LAW AND PRACTICE (50 MARKS)

5. Introduction

Special features of indirect tax levies—all pervasive nature, contribution to Government revenues; constitutional provisions authorizing the levy and collection of duties of central excise, customs, service tax, central sales tax and VAT.

6. Central Excise Laws

Basis of chargeability of duties of central excise - goods, manufacture, classification and valuation of excisable goods, CENVAT; assessment procedure, exemption, payment, recovery and refunds of duties.

Clearance of excisable goods; Central Excise Bonds; maintenance of accounts and records and filing of returns.

Duties payable by small scale units. set-off of duties – concept, meaning and scheme; Central Excise Concessions on exports; search, seizure and investigation; offences and penalty.

Adjudication, Appeal and Revision, including appearance before CEGAT by Company Secretary as authorised representative; settlement of cases.

7. Customs Laws

Levy of and exemption from, customs duties – specific issues and case studies; assessment and payment duties; recovery and refund of customs duties.

Procedure for clearance of imported and exported goods; drawback of duties.

Transportation and warehousing

Confiscation of goods and conveyances and imposition of penalties; search, seizure and arrest, offences and prosecution provisions.

Adjudication, Appeal and Revision; Settlement of Cases.

8. Promissory Estoppel in Fiscal Laws – principles and applicability with reference to indirect taxes.

9. Tax Planning and Management – scope and management in customs, with specific reference to important issues in the respective areas.

PART-C: INTERNATIONAL TAXATION (20 MARKS)

10. Basic Concepts of International Taxation

Residency issues; source of income; tax havens; unilateral relief and Double Tax Avoidance; transfer pricing; international merger and acquisitions; impact of tax on GATT 94, WTO, anti dumping processing; the subpart F Regime : definition of CFC, Subpart F Income and Operating Rules.

11. Advance Ruling and Tax Planning

Authority for advance rulings, its power and procedure; applicability of advance ruling; application for advance ruling and procedure on receipt of application.

Tax planning and special provisions relating to certain incomes of non-resident corporate assessee.

Double taxation avoidance agreements; general principles; provisions and tax implications thereof.

12. Taxation of Inbound Transactions

Taxation of passive investments; capital gains and losses; income taxation; property taxation; branch profit taxation

13. Taxation of Outbound Transactions

Foreign tax credit; foreign income exclusions; indirect foreign tax credit (deemed paid system vs. current pooling system); Controlled Foreign Corporations; PFIC's (Passive Foreign Investment Companies); cross border merger, acquisitions and transfers.

LIST OF RECOMMENDED BOOKS
ADVANCED TAX LAWS AND PRACTICE

Readings:

I. Direct Taxes

1. Girish Ahuja & Ravi Gupta : Corporate Tax Planning and Management, Direct Tax Law & Practice : Bharat Law House (P) Ltd. 22, Tarun Enclave, Pitampura, New Delhi-110 034.
2. E A Srinivas : Corporate Tax Planning; McGraw Hill Education (India) Ltd., B-4, Sector-63, Noida – 201 301.
3. Income Tax Act & Rules : Bare Act
4. Wealth Tax Act & Rules : Bare Act
5. Annual Finance Act
6. Company Law Journal
7. Corporate Law Adviser
8. H P Ranina : Corporate Taxation – A Hand Book; Orient Law House, Allahabad.

II. Indirect Taxes

1. V S Datey : Indirect Taxes – Law & Practices; Taxmann Publications, 59/32, New Rohtak Road, New Delhi-110 055.
2. V Balachandran : Indirect Taxation, Sultan Chand & Sons, 23, Daryaganj New Delhi-110 002
3. Dr. Sanjeev Kumar : Systematic Approach to Indirect Taxes, Bharat Law House, 22, Tarun Enclave, Pitampura, New Delhi - 110 034.
4. S P Bhatnagar : Customs Law & Procedure; Centax Publications, Defence Colony, 1512-B, Sachdeva P.T. College of Defence Colony, New Delhi – 110 003
5. Acharya Shuklendra : Central Excise — Law, Practice & Procedure; Modern Law House, 1/1, A.D.A. Flat (near Bishop Johnson School), M.G. Marg, Allahabad – 211 001

III. International Taxation

1. Carl Fonntag & C.S.Mathur : Principles of International Taxation, Butterworths, Lexis Nexis (Butterworths), 14th Floor, Vijaya Building, 17, Barakhamba Road, New Delhi – 110001
2. S C Mishra : Transfer Pricing Manual
3. Roy Rohatgi : Basic International Taxation, Kluwer Law International Ltd., Sterling House, 66 Wilton Road, London SW1V 1DE, United Kingdom/In India – Taxmann Publication (P) Ltd., 59/32, New Rohtak Road, New Delhi-110005.

References:

I. Direct Taxes

1. Dr. V K Singhania : Direct Taxes — Law and Practices; Taxmann Publications (P) Ltd; 59/32, New Rohtak Road, New Delhi – 110 005.
2. Dr. B B Lal : Direct Taxes; Konark Publications (P) Ltd., A-149, Main Vikas Marg, Delhi – 110 092.

II. Indirect taxes

3. Kanga & Palkhivala : The Law and Practice of Income Tax; N M Tripathi (P) Ltd.
4. Taxmann : CENVAT Law & Practice; Taxmann Allied Services (P) Ltd., 59/32, New Rohtak Road, New Delhi – 110005
5. S D Majumdar : Customs Valuation – Law and Practice; Centax Publications Pvt Ltd. 1512-B, Sachdeva P.T. College of Defence Colony, New Delhi – 110 003
6. G Sarangi : Central Excise Guide for Small Scale Industry, Centax Publications Pvt Ltd. 1512-B, Sachdeva P.T. College of Defence Colony, New Delhi – 110 003
7. S R Roy : Commentaries on Customs Act; Kamal Law House, 8/2, K.S. Roy Road, Calcutta – 700 001
8. Gupta & Ahuja : Professional Approach to Direct Taxes- Law and Practice.

(x)

Journals

1. Chartered Secretary : ICSI, New Delhi
2. Student Company Secretary : ICSI, New Delhi
3. Income Tax Reports : Company Law Institute of India (P) Ltd., Chennai.
4. Taxmann : Taxmann Publications (P) Ltd.; 59/32, New Rohtak Road, New Delhi – 110 005.
5. Tax and Corporate : Referencer, Bharat Law House (P) Ltd., 22, Tarun Enclave, Pitampura, New Delhi-110 034.
6. Excise and Customs Cases : Fortnightly Reporting Journals; Indirect Tax Laws of India (P) Ltd., Chennai.
7. Excise Law Times : Fortnightly Reporting Journal; Centax Publications (P) Ltd.1512-B, Sachdeva P.T. College of Defence Colony, New Delhi – 110 003

BRIEF-CONTENTS

<i>Study Lesson No.</i>	<i>Topic</i>
Part A –Direct Taxation—Law and Practice	
I.	General Framework of Direct Taxation In India
II.	Companies under Income Tax Laws
III.	Tax Planning
IV.	Tax Management
Part B – Indirect Taxation—Law and Practice	
V.	Introduction
VI.	Central Excise Laws
VII.	Custom Laws
VIII.	Promissory Estoppel in Fiscal Laws
IX.	Tax Planning and Financial Management Decisions
Part C – International Taxation	
X.	Basic Concepts of International Taxation
XI.	Advance Ruling and Tax Planning
XII.	Taxation of Inbound Transactions
XIII.	Taxation of Outbound Transactions
TEST PAPERS	
Question Paper Set of Two Previous Sessions	

(xiii)

PROFESSIONAL PROGRAMME
ADVANCED TAX LAWS AND PRACTICE

C O N T E N T S

PART A –DIRECT TAXATION—LAW AND PRACTICE

STUDY I

GENERAL FRAMEWORK OF DIRECT TAXATION IN INDIA

	<i>Page</i>
Learning Objectives	...
1.1 Introduction and Constitutional Provisions	1
1.2 Finance Acts	5
1.3 Tax liability under different Acts	5
Lesson Round-up	6
SELF-TEST QUESTIONS	6

STUDY II

COMPANIES UNDER INCOME TAX LAWS

Learning Objectives	...
2.1 Constitutional Provisions	7
2.2 Meaning of Company under Section 2(17) of Income Tax Act	7
2.3 Categories of Companies under the Income Tax Act, 1961	9
2.3.1 Indian Company	9
2.3.2 Domestic Company	10
2.3.3. Foreign Company	11
2.3.4 Company in which public are substantially interest (a widely held company)	11
2.3.5 Closely held company	12
2.4 Tax incidence under Income Tax Act, 1961	13
2.5 Rates of Income Tax for Assessment Year 2012-13	14
2.6 Minimum Alternate Tax (MAT)	15
2.6.1 Meaning of “Book Profit”	16
2.6.2 MAT Credit	18
2.7 Dividend Distribution Tax u/s 115O	19
Lesson Round-up	20
SELF-TEST QUESTIONS	20

STUDY III

TAX PLANNING

Learning Objectives	...
3.1 Concept of Tax Planning	22

This Study Paper is the property of the Institute of Company Secretaries of India. Permission of the Council of the Institute is essential for reproduction of any portion of the Paper.

	<i>Page</i>
3.2 Tax Planning, Tax Avoidance and Tax Evasion	... 24
3.3 Objectives of Tax Planning	... 26
3.4 Importance of Tax Planning	... 27
3.5 Diversion of Income and Application of Income	... 28
3.6 Essentials of Tax Planning	... 29
3.7 Types of Tax Planning	... 29
3.8 Areas of Tax Planning in the context of Income Tax Act, 1961	... 30
3.8.1 Form of the organization	... 30
3.8.2 Locational Aspects	... 36
3.8.3 Nature of Business	... 36
3.8.4 Tax Planning Relating to Corporate Restructuring	... 37
3.8.5 Tax Planning Relating to Financial Management Decisions	... 39
3.8.6 Tax Planning Relating Non-residents	... 40
3.8.7 Tax Planning for Indian Collaborators	... 42
3.8.8 Tax Planning for Employees	... 43
3.8.9 Tax Planning under Wealth Tax Act	... 44
3.9 Planning in the context of Court Rulings and Legislative Amendments	... 44
3.10 Statutory force of the Notifications	... 45
3.11 Organization of Tax Planning Cells	... 46
3.12 Overall Tax Planning Measures	... 48
3.13 Some General Considerations Regarding New Business	... 49
3.14 Setting-up and Commencement of Business vis-à-vis	
Tax Planning	... 51
Lesson Round-up	... 54
SELF-TEST QUESTIONS	... 54

**STUDY IV
TAX MANAGEMENT**

Learning Objectives	... 56
4.1 Introduction	... 56
4.2 Filing of Income-tax Returns	... 56
4.3 Defaults and Penalties	... 58
4.4 Appeals and Revisions	... 63
4.4.1 Right of Appeal	... 63
4.4.2 Appellate Authorities	... 63
4.4.3 Appealable orders before Commissioner (Appeals) (Section 246A)	... 64
4.4.4 Procedure for filing of appeal (Section 249(1))	... 65
4.4.5 Period of limitation to prefer an appeal (Section 249(2))	... 66
4.4.6 Revision by the Commissioner of Income Tax (Sections 263 and 264)	... 68

	<i>Page</i>
4.4.7 Revision by orders prejudicial to the interest of revenue (Sections 263)	... 69
4.4.8 Revision of order in the interest of Assessee (Sections 264)	... 72
4.4.9 Remedy against the revisional order	... 74
4.5 Appellate Tribunal (Section 252)	... 74
4.6 Appeal to High Court	... 79
4.7 Appeal to the Supreme Court (Section 261)	... 80
4.8 Alternate Dispute Resolution Mechanism	... 81
Lesson Round-up	... 81
SELF-TEST QUESTIONS	... 82

PART B—INDIRECT TAXATION—LAW AND PRACTICE

STUDY V

INTRODUCITON

Learning Objectives	... 83
5.1 Introduction	... 83
5.2 Constitutional Provisions	... 83
5.3 Central Excise	... 84
5.4 Customs Law	... 85
5.5 Central Sales Tax Act	... 86
5.6 Service Tax	... 86
5.6.1 Constitutional Validity	... 87
5.6.2 Scope	... 88
5.6.3 Computation of Tax	... 88
5.7 Value Added Tax (VAT)	... 89
5.7.1 Methods of Computation	... 92
5.7.2 Procedure	... 93
5.7.3 Rates of Tax	... 93
Lesson Round-up	... 93
SELF-TEST QUESTIONS	... 94

STUDY VI

CENTRAL EXCISE LAWS

Learning Objectives	... 95
6.1 Basis of Levy of Excise Duties	... 96
6.2 Basis of chargeability of Excise Duty	... 96
6.2(a) The Concepts of "Goods"	... 98
- Movability	... 100
- Marketability	... 102
- Related Concepts of goods under Central Excise	... 104

	<i>Page</i>
6.2(b) The Concept of 'Excisable Goods'	... 106
6.2(c) Production, Manufacture and Process Distinguished	... 107
- Concept of Manufacture	... 107
- Judicial Pronouncements on the Concept of Manufacture	... 108
- Processes specified in Central Excise Tariff Act, 1985 Amounting to Manufacture/Deemed Manufacture	... 112
6.2(d) Concept of "Manufacturer"	... 113
- Tests of a Manufacturer	... 115
- Latest Cases of Manufacture and Goods	... 117
6.3 Classification of Goods	... 118
6.4 Valuation of Goods under Central Excise Law	... 124
6.4.1 Methods of Valuation	... 126
6.4.1(a) Valuation Based on MRP [Retail Sale Price](Section 4A)	... 126
6.4.1(b) Scope and Objects	... 127
6.4.1(c) Concept of Transaction Value	... 128
6.4.2 Procedure for Fixation of Value under Section 4	... 129
- Valuation Rules	... 132
- Valuation under Job Work	... 139
-The Central Excise Valuation (Determination of Price of Excisable Goods) Rules, 2000	... 140
- The Central Excise (Determination of Retail Sale Price of Excisable Goods) Rules, 2000	... 142
6.5 Payment of Excise Duties	... 143
6.6 Clearance and Removal Procedures	... 145
6.6.1 Self Assessment Method	... 145
6.6.2 Removal of Goods on Invoice	... 146
6.6.3 Compounded Levy Scheme	... 147
6.7 Remission of Duty (Rule 21)	... 148
6.8 Assessment	... 148
6.9 Filing of Return	... 150
6.10 Large Tax Payer Units	... 150
6.11 Excise Duty - Exemptions	... 151
6.12 Recovery of Sums Due to Government (Section 11)	... 157
6.13 Recovery of Dutie not Levied or not Paid or Short Levied or Short Levied or Short Paid or Erroneously Refunded (Section 11A)	... 157
6.14 Interest on delayed payment of duty (Section 11AA)	... 159
6.15 Claim for Refunds of Duty and interest, if any, paid on such duty (Section 11B)	... 159

(xvii)

	<i>Page</i>
6.16 Doctrine of unjust enrichment	... 161
6.17 Payment of interest on delayed Refund (Section 11BB)	... 161
6.18 Power not to recover duty of excise not levied or short levied as a general Practice (Section 11C)	... 161
6.19 Excise Audit—2000	... 162
6.20 Deposit of Central Excise Duty during strikes in Nominated Banks	... 163
6.21 Appellate Procedures and Search, Seizure and Investigation	... 165
6.21.1 Appellate Scheme	... 166
6.21.2 Appeals before Commissioner (Appeals)(Section 35)	... 166
6.21.3 CESTAT	... 168
6.21.4 Further Remedies after Decision by CESTAT	... 172
6.21.5 Power of Committee of Chief Commissioner of Central Excise or Commissioner of Central Excise to pass certain Orders on its own (Section 35E)	... 174
6.21.6 Deposit Pending appeals of duty demanded or Penalty levied (Section 35F)	... 174
6.21.7 Interest on delayed refund of amount deposited under Proviso to Section 35F (Section 35FF)	... 175
6.21.8 Revisionary Role of the Central Government	... 175
6.22 Settlement Commission	... 176
6.22.1 Power of Commission	... 176
6.22.2 Application to the Commission	... 177
6.22.3 Procedure	... 178
6.23 Power and duties of officers	... 178
6.23.1 Access to a registered premises (Rule 22)	... 180
6.23.2 Power to stop and search (Rule 23)	... 180
6.23.3 Return of Records (Rule 24A)	... 180
6.23.4 Power to detain goods or seize the goods (Rule 24)	... 180
6.23.5 Confiscation and Penalty (Rule 25)	... 181
6.23.6 Penalty for certain offences (Rule 26)	... 181
6.23.7 On confiscation, property to vest in the Central Government (Rule 28)	... 181
6.23.8 Disposal of goods confiscated (Rule 29)	... 182
6.23.9 Storage charges in respect of goods confiscated and redeemed (Rule 30)	... 182
6.24 Power of Adjudication (Section 33)	... 182
6.24.1 Option to pay fine in lieu of Confiscation (Section 34)	... 182
6.24.2 Confiscation and penalty not to interfere with other punishments (Section 34A)	... 183
6.25 Procedure to be followed in cases where duty is paid under Protest	... 183

	<i>Page</i>
6.26 Special audit in certain cases (Section 14A) ...	183
6.27 Special audit in cases where credit of duty availed or utilized is not within the normal limits etc. (Section 14AA) ...	184
6.28 CENVAT Credit Rules, 2004 ...	185
6.29 Small Scale Industries – Exemption & Concessions ...	206
6.30 Conclusion ...	213
Lesson Round-up ...	216
SELF-TEST QUESTIONS ...	217

**STUDY VII
CUSTOM LAWS**

Learning Objectives ...	219
7.1 Introduction ...	220
7.2 Taxable Event ...	221
7.3 Types of Duties under Customs ...	223
7.4 Tariff Classification ...	226
7.4.1 Computation of the (i) Basic Customs Duty (ii) surcharge (iii) Additional Duty of Customs; (iv) Special Additional Duty under the Customs Tariff Act, 1975 and other Laws ...	226
7.5 Valuation of Goods for levy of Customs Duty ...	228
7.5.1 Section 14 : Valuation of Goods for Purposes of Assessment ...	229
7.5.2 Customs Valuation (Determination of Price of Imported Goods) Rules, 2007 ...	230
7.6 Valuation of Export Goods ...	238
7.6.1 Custom Valuation (Determination of Value of Exports Goods) Rules, 2007 ...	238
7.7 Determination of Rate of Duty and Tariff Valuation ...	242
7.8 Remission, Exemption and Demands in Customs ...	244
7.8.1 Duty on Pilfered Goods ...	244
7.8.2 Re-Importation of Goods ...	245
7.8.3 Goods derelict, wreck etc. ...	246
7.8.4 Abatement of Duty ...	246
7.8.5 Remission of duty on cost, destroyed or abandoned goods ...	247
7.8.6 Denaturing or Mutilation of Goods (Section 24) ...	247
7.8.7 Exemption from Duty ...	248
7.8.8 Policy Guidelines for ad hoc exemptions under Section 25(2) ...	250
7.8.9 Refund of Duties ...	251
7.9 Recovery of duties ...	255
7.10 Recovery of Duties not levied or short levied or erroneously Refunded ...	258
7.11 Power not to recover duties ...	259

	<i>Page</i>
7.12 Interest on Delayed Payment of Duty	... 260
7.13 Recovery of duties in certain cases (Section 28AA)	... 260
7.14 Assessment of Duty (Section 17)	... 261
7.15 Provisional Assessment of Duty	... 262
7.16 Advance Ruling	... 264
7.17 Clearance of Imported or Exported Goods including Baggage	... 266
7.17.1 Clearance of Import Cargo	... 266
7.17.2 Imported Goods—Provisions in the Customs Act, 1962	... 267
7.17.3 Procedure for clearance of the goods	... 268
7.18 Assessable Value and Levy of Duty—Method of Assessment	... 278
7.19 Penal Action	... 279
7.20 Clearance of Export Cargo	... 280
7.21 Customs Procedure—Documentation for Export	... 282
7.22 Shipment (Export) under claim for Drawback	... 286
7.23 Procedure for Exports through inland container depots	... 287
7.24 Procedure for Exports of containerized Cargo from Inland Container Depots	... 290
7.25 Baggages	... 291
7.25.1 Temporary Detention of Baggage	... 292
7.25.2 Regulation in respect of Baggage	... 292
7.26 Goods Imported or Exported by Post	... 293
7.27 Stores	... 296
7.28 Provisions Relating to Coastal Goods and Vessels Carrying Coastal Goods	... 299
7.29 Duty Drawback	... 302
7.29.1 Statutory Provisions in the Customs Act, 1962	... 303
7.29.2 Section 74 of Customs Act, 1962—Drawback allowable on re-export of duty (Customs Import Duty) paid goods	... 303
7.30 Transportation of Goods	... 311
7.31 Warehousing	... 315
7.32 Adjudication and Appellate Provisions	... 328
7.32.1 Appellate Procedures	... 329
7.33 Power of Committee of Chief Commissioners of Customs or Commissioners of Customs to pass certain order	... 335
7.34 Section 129DD, Revision by Central Government	... 336
7.35 Section 130E, Appeal to Supreme Court	... 337

(xx)

	<i>Page</i>
7.36 Section 129E, Deposit, pending appeal of duty and interest demanded or penalty levied ...	337
7.37 Section 129EE: Interest on delay Payment of Refund ...	338
7.38 Section 131, Sums due to be paid notwithstanding reference etc. ...	338
7.39 Section 131A, Exclusion of time taken for copy ...	338
7.40 Section 131B, Transfer of certain pending proceedings and Transitional Provisions ...	338
7.41 Appeal not to be filed in certain cases (Section 131BA) ...	339
7.42 Customs (Appeals) Rules, 1982 ...	340
7.43 Settlement Commission ...	344
7.43.1 Customs and Central Excise Settlement Commission Procedure, 2007 ...	345
7.44 Search, Seizure, Arrest, Confiscation etc. ...	349
7.45 Confiscation of Goods ...	355
7.46 Adjudication of Confiscation and Penalties ...	362
7.47 Option to pay fine in lieu of Confiscation ...	363
7.48 Award of Confiscation or Penalty by Customs Officers not to Interfere with other Punishment ...	364
7.49 Offences and Prosecution Provisions ...	366
7.50 Miscellaneous Provisions ...	372
Lesson Round-up ...	383
SELF-TEST QUESTIONS ...	384

STUDY VIII

PROMISSORY ESTOPPEL IN FISCAL LAWS

Learning Objectives ...	389
8.1 Promissory Estoppel in Fiscal Laws ...	389
8.1.1 Doctrine of Promissory Estoppel under Tax Laws ...	390
8.2 Customs Act and Tax Planning ...	392
8.3 Excise Law and Tax Planning ...	400
8.4 CENVAT ...	403
Lesson Round-up ...	405
SELF-TEST QUESTIONS ...	405

STUDY IX

TAX PLANNING AND FINANCIAL MANAGEMENT DECISIONS

Learning Objectives ...	406
9.1 Scope and Management in Customs ...	406
9.2 Scope ...	407
9.3 Customs Officials ...	407

	<i>Page</i>
9.4 Exemption from Duty	... 408
9.5 Refunds	... 409
9.6 Authorities for Advance Rulings	... 409
9.7 Clearance of Import & Export Duties	... 409
9.8 Warehousing	... 410
9.9 Customs Duty Drawback	... 411
9.10 Baggage Rules	... 411
Lesson Round-up	... 416
SELF-TEST QUESTIONS	... 417

PART C—INTERNATIONAL TAXATION

STUDY X

BASIC CONCEPTS OF INTERATIONAL TAXATION

Learning Objectives	... 418
10.1 An Overview—from Indian Perspective	... 418
10.2 Tax Haven	... 420
10.2.1 Determining Factors of Tax Haven	... 420
10.2.2 Methodology	... 421
10.2.3 Action taken to avoid Harmful Tax Practices	... 422
10.3 Controlled Foreign Corporation (CFC)	... 422
10.4 Sub Part F	... 423
10.5 Meaning of the term 'Resident of Contracting State'	... 425
10.6 Double Taxation Relief	... 426
10.7 Necessity for DTAA	... 429
10.7.1 Taxation of Income from Air and Shipping Transport under DTAA	... 430
10.7.2 The Concept of Permanent Establishment (PE)	... 431
10.8 Transfer Pricing	... 432
10.9 Taxation Aspect of International Merger and Acquisitions	... 458
10.10 Acquisition	... 459
Lesson Round-up	... 462
SELF-TEST QUESTIONS	... 462

STUDY XI

ADVANCE RULING AND TAX PLANNING

Learning Objectives	... 463
11.1 Concept of Advance Ruling	... 463
11.1.1 Who can seek Advance Ruling	... 464

(xxii)

	<i>Page</i>
11.1.2 Authority for Advance Ruling : Concept of Advance Ruling And Creation of Authority for Advance Ruling	... 464
11.1.3 Application for Advance Ruling	... 465
11.1.4 Powers of the Authority	... 467
11.1.5 Applicability of Advance Ruling (Section 245-S)	... 468
Lesson Round-up	... 469
SELF-TEST QUESTIONS	... 469

STUDY XII

TAXATION OF INBOUND TRANSACTIONS

Learning Objectives	... 470
12.1 What is Inbound and Outbound Transaction	... 470
12.2 Taxation of Passing Investments	... 471
12.3 Inbound Investment Strategies	... 471
12.4 Entry Options for Foreign Companies	... 473
12.5 Foreign Direct Investment	... 474
12.6 Automatic Route	... 474
12.7 Government Approval	... 475
12.8 Reforms in the Foreign Investment Regime	... 476
12.8.1 New Press Note Concerning FDI	... 476
12.8.2 Withholding Tax for NRIs and Foreign Companies	... 477
12.9 Tax on Income of Foreign Institutional Investors from Securities or Capital Gains Arising from their Transfer (Section 115AD)	... 478
12.10 Property and Capital Gain Tax (Relating to Securities)	... 479
12.11 Long-term Capital Gains in respect of Shares, Securities and Units (Section 112)	... 480
12.12 Branch Profit Taxation	... 481
Lesson Round-up	... 482
SELF-TEST QUESTIONS	... 482

STUDY XIII

TAXATION OF OUTBOUND TRANSACTIONS

Learning Objectives	... 483
13.1 Foreign Tax Credit	... 483
13.2 Case Laws	... 485
13.3 Tax Exclusions (Exemptions) with respect to foreign income	... 486

	<i>Page</i>
13.4 Outward Investment Strategies	... 487
13.5 Surcharge on Income Tax (In the Case of Companies)	... 488
13.6 Passive Foreign Investment Company (PFIC)	... 488
Lesson Round-up	... 491
SELF-TEST QUESTIONS	... 492
TEST PAPERS 2012	... 493
Test Paper 1/2012	... 495
Test Paper 2/2012	... 496
Test Paper 3/2012	... 499
Test Paper 4/2012	... 503
Test Paper 5/2012	... 507
QUESTION PAPER OF TWO PREVIOUS SESSIONS	... 511

PROFESSIONAL PROGRAMME

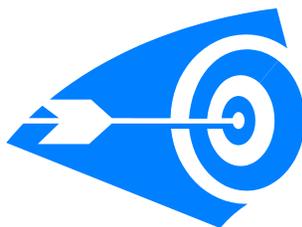
ADVANCED TAX LAWS AND PRACTICE

PART A –DIRECT TAXATION—LAW AND PRACTICE

STUDY I

GENERAL FRAMEWORK OF DIRECT TAXATION IN INDIA

LEARNING OBJECTIVES



This objective of the study lesson is to enable the students to understand:

- Constitutional Provisions relating to Tax Laws
- Finance Act
- Tax obligations under different acts and harmonisation of tax regime

1.1 INTRODUCTION AND CONSTITUTIONAL PROVISIONS

India is a federal union of states with distribution of powers. Articles 245 to 255 of the Constitution of India relate to legislative relations between the Union and the States in the form of federal distribution of legislative powers between the Parliament and the Legislature of a State. These powers to make laws are conferred by Articles 245, 246 and 248 whereas the subject matters of laws to be made by the Parliament and the legislatures of States are listed in Schedule VII to the Constitution.

There is a threefold distribution of legislative powers as stipulated in Article 246 read with Schedule VII. List I of the Union list in Schedule VII comprises of 99 items or subjects over which the Union shall have the exclusive powers of legislation. List II of the State list comprises of 61 items over which the State Legislature shall have the exclusive powers of legislation. List III of the concurrent list comprises of 52 items over which the Parliament and the Legislatures of States shall have concurrent powers. These three lists demarcate the fields of legislation whereas the powers of legislation are conferred by Article 246.

The Union list includes citizenship, Railways, major ports and airways, trade and commerce with foreign countries, defence, foreign affairs, banking, insurance, currency and coinage, taxes on income other than agricultural income, duties of customs, duties of excise on tobacco and other goods manufactured or produced in India except alcoholic liquor for human consumption, opium etc. corporation tax, taxes on capital value of assets other than agricultural land, taxes on the capital of companies, estate duty in respect of property other than agricultural land etc.

The State list includes public order and police, local government, public health and sanitation, agriculture, forests and fisheries, education, taxes on agricultural income duties in respect of succession to agricultural land, taxes on lands and buildings, taxes on sale and purchase of goods other than newspapers, toll taxes on professions, trades, callings and employments taxes on luxuries including taxes on entertainment, amusement, betting and gambling. The Concurrent list includes Civil and Criminal law and procedure, marriage, contracts, trusts, labour welfare, education, charities and charitable institutions, price control, electricity etc.

The distribution of fields of taxes duties etc. between the Union and the States as earmarked in Schedule VII is summarized hereunder:

Union List

1. Taxes on income other than agricultural income;
2. Corporation tax;
3. Custom duties;
4. Excise duties except on alcoholic liquors and narcotics not contained in toilet and medical preparations;
5. Estate and succession duties other than on agricultural land;
6. Taxes on the capital value of the assets; except agricultural land' of individual and companies;
7. Rates of stamp duties on financial documents;
8. Taxes other than stamp duties on transactions in stock exchanges and future markets;
9. Taxes on sale or purchase of newspapers and on advertisements published therein;
10. Taxes on railway freight and fares;
11. Terminal taxes on goods or passengers carried by railways, sea or air; and
12. Taxes on the sale or purchase of goods in the course of inter-State trade.

State List

1. Land revenue;
2. Taxes on the sale and purchase of goods, except newspapers;
3. Taxes on agricultural income;
4. Taxes on land and buildings;
5. Succession and estate duties on agricultural land;
6. Excise on alcoholic liquors and narcotics;
7. Taxes on the entry of goods into a local area;
8. Taxes on mineral rights, subject to any limitations imposed by Parliament;
9. Taxes on consumption and sale of electricity;
10. Taxes on vehicles, animals and boats;

11. Stamp duties except those on financial documents;
12. Taxes on goods and passengers carried by road or inland water ways;
13. Taxes on luxuries including entertainment, betting and gambling;
14. Tolls;
15. Taxes on professions, trades, callings and employment;
16. Capitation taxes; and
17. Taxes on advertisement other than those contained in newspapers.

The Central Government has exclusive power to impose taxes which are not specifically mentioned in the State or Concurrent lists. The Union and the State Governments have concurrent powers to fix the principles on which taxes on motor vehicles shall be levied and to impose stamp duties on non-judicial stamps. The property of the Central Government is exempted from State taxation and the property and income of the States are exempted from Union taxation.

Article 265 provides that no tax shall be levied or collected except by authority of law. Thus, the tax proposed to be levied or collected must be within the legislative competence of the legislature imposing the tax. Tax includes duties, cesses or fees by way of general, special or local imposts. The law imposing the tax, like other laws, must not violate any fundamental right or contravene any specific provision relating to particular matters e.g. the prohibition against specific appropriation of the proceeds of any tax in payment of expenses for the promotion or maintenance of any particular religious denomination (Article 27) or the ceiling of ₹ 2500 per annum in respect of total amount payable by one person as taxes on profession, trade, calling or employment (Article 276(2)) or the specific restrictions on the imposition of sales tax by a State (Article 286) or the freedom of trade and commerce carried on between one place and another in India so as to ensure that the economic unity of India is not broken up by internal barriers (Article 301).

A law to levy or collect any tax or duty or cess or fees does not include an executive order or a rule without express statutory authority. A Money Bill, which includes a bill to impose, abolish, remit, alter or regulate any tax shall not be introduced in Rajya Sabha or a legislative council. Such a Bill shall not be moved or introduced except as the recommendations of the President or the Governor, as the case may be.

Articles 268 to 281 relate to the distribution of revenues between the Union and States. Stamp duties like those on financial documents and excise or medicinal or toilet preparations as mentioned in the Union list are to be levied by the Government of India but are to be collected by the States (Article 268). Taxes on inter-State trade or commerce by way of sale or purchase of goods and taxes on the consignment of goods are to be levied and collected by the Government of India but are to be assigned to the States (Article 269). All taxes and duties referred to in the Union list, except those referred to in Articles 268 and 269, surcharge on taxes and duties, for the purposes of the Union and any cess levied by the Parliament for specific purposes are to be collected by the Government of India and are to be distributed between the Union and the States in the manner prescribed by the President by

order until a Finance Commission has been constituted and after its constitution, as prescribed by the President by order after considering the recommendations of the Finance Commission.

Article 274 stipulates that prior recommendation of President is required to Bills affecting taxation in which States are interested.

“No bill or amendment which imposes or varies any tax or duty in which States are interested, or which varies the meaning of the expression “agricultural income” as defined for the purposes of the enactments relating to Indian Income Tax, or which affects the principles on which under any of the foregoing provisions of this Chapter, moneys are or may be distributable to States, or which imposes any such surcharge for the purposes of the Union as is mentioned in the foregoing provisions of this Chapter, shall be introduced or moved in either House of Parliament except on the recommendation of the President.

The expression tax or duty in which States are interested in this Article means : (a) a tax or duty the whole or part of the net proceeds whereof are assigned to any State, or (b) a tax or duty by reference to the net proceeds where of sums are for the time being payable out the Consolidated Fund of India to any State.”

The plain reading of above Article 274 clearly stipulates that before any Finance Bill can be moved in either House of Parliament, a prior recommendation from President is required.

Income tax being direct tax happens to be the major source of revenue for the Central Government. The entire amount of income tax collected by the Central Government is classified under the head: (a) Corporation Tax (Tax on the income of the companies) and (b) Income Tax (Tax on income of the non-corporate tax assesseees).

This classification of Income Tax in to : (a) Corporation Tax; and (b) Income Tax, is of great assistance to the Central Government while preparing budget estimates and setting the target. The classification of Income Tax in to above two categories is also important for easy division of income tax between the Central and State Governments as the proceeds from Corporation Tax are not divisible with the States [Article 270(1) read with Article (4)(a)].

Municipality or other local authority or body for the purposes of the State, district or other local area may, notwithstanding that those taxes, duties, cesses or fees are mentioned in the Union List, continue to be levied and to be applied to the same purposes until provision to the contrary is made by Parliament by law.”

As per recommendations of the Eleventh Finance Commission duly accepted by the Government, in the overall scheme of transfer of funds, 37.5% of the gross revenue receipts is the ceiling for such transfer of funds to the States. This includes (i) 28% of the net proceeds of shareable central taxes and duties to the States; (ii) 1.5% of the net proceeds of shareable Central taxes in lien of sales tax on sugar, tobacco and textiles, and (iii) grant-in-aid to States facing revenue deficits after devolution, grants, meant for local bodies and grants for calamity relief. It has also laid down the criteria for determining relative shares of States in central pool of taxes

and duties which is based on the weightage given to population area index of infrastructure, tax effort and fiscal discipline.

1.2 FINANCE ACTS

The Income Tax Act 1961 relates to the direct tax aspect of the taxation regime in the country. The Act contains all provisions regarding taxation under different heads of income.

The finance bill passed by the Parliament after it is being tabled and necessary recommendation/amendments has been made in it. It is usually presented in the parliament by the Finance Minister.

Once the bill has been passed by the parliament after necessary amendments, then it goes to the President for his assent. The bill becomes an Act after the President has assented to it. The effective date is usually mentioned in the notification in the official gazette or in the Act itself.

Regarding indirect taxes, the ad valorem tax rates are effective from the midnight of the date of presentation of the Union Budget.

The Finance Act contains necessary amendments in the Income Tax Act signifying the policy decisions of the Union government regarding the financial matters.

The Finance Bill is usually presented in the last week of February every year.

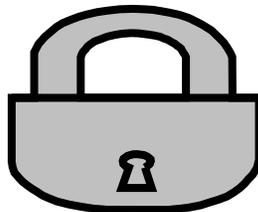
1.3 TAX LIABILITY UNDER DIFFERENT ACTS

A business transaction can give rise to liability to tax under the different tax Acts in various ways. All these Acts contain certain deeming provisions, which envisage some sort of clubbing of income/wealth belonging to others. Under the Income Tax Act, for example, though it is the total income of the assessee, which is chargeable to tax, but under certain circumstances, the income of other persons is sought to be included in the assessee's total income (Sections 60 to 64). Similarly, under the Wealth Tax Act, 1957 it is the net wealth of the assessee excluding the exemption limit which attracts tax. In computing the net wealth of the assessee as on the valuation date relevant for the assessment year, certain assets transferred by the assessee without suitable consideration and held by the specified categories of persons are also sought to be included under Section 4 of the Wealth Tax Act, 1957. Thus, the same transaction could give rise to tax liability under different Acts under different circumstances. For instance, a transfer might be complete under the general law, still if the transfer without consideration is made, say, to the spouse of the transferor, the income arising from the transferred assets will continue to be taxed in the hands of the transferor for income tax purposes and the value of the properties will continue to be included in the net wealth of the transferor for Wealth Tax purposes. This is because one of the modes by which levy of tax can be avoided is by transferring income-earning assets to near and dear ones.

The above analysis shows that there exists an intimate relationship between the various Direct tax Acts and that under certain circumstances the assessee will not stand to gain from tax point of view even by transferring the property to others. Of course, there are some provisions in some of these Acts which seek to provide some sort of relief in respect of the tax paid under one or more of the legislations.

LESSON ROUND UP

- Article 265 provides that no tax shall be levied or collected except by authority of law. Thus, the tax proposed to be levied or collected must be within the legislative competence of the legislature imposing the tax. Tax includes duties, cesses or fees by way of general, special or local imposts.
- The Finance Act contains necessary amendments in the Income Tax Act signifying the policy decisions of the Union government regarding the financial matters.
- Article 274 clearly stipulates that before any Finance Bill can be moved in either House of Parliament, a prior recommendation from President is required.
- Income tax being direct tax happens to be the major source of revenue for the Central Government. The entire amount of income tax collected by the Central Government is classified under the head: (a) Corporation Tax (Tax on the income of the companies) and (b) Income Tax (Tax on income of the non-corporate tax assesses).

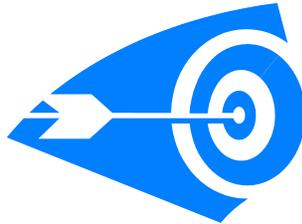
SELF-TEST QUESTIONS

(These questions are meant for recapitulation only. Answers to these questions are not to be submitted for evaluation)

1. Discuss the constitutional provisions relating to levying of taxes by the Centre and State Government.
 2. Discuss the importance of classifying the Income tax between Corporation and Income Tax. How is the Income tax collected by the Central Government shared between the Centre and various State Governments?
 3. What are different direct tax laws in force in our country? How far are they interrelated in the scheme of Indian taxation system?
 4. Explain the importance of the Income Tax Act, 1961 in India and its relationship with the Annual Finance Acts.
-

STUDY II
COMPANIES UNDER INCOME TAX LAWS

LEARNING OBJECTIVES



The objective of the study lesson is to enable the students to understand:

- Constitutional provisions
- Meaning of Company under section 2(17) of the Income-tax Act
- Categories of companies under the Income-tax Act, 1961
- Tax incidence under Income-tax Act, 1961
- Rates of Income Tax for Assessment Year 2013-14
- Minimum Alternate Tax (MAT)
- Dividend Distribution Tax u/s 115O

2.1 CONSTITUTIONAL PROVISIONS

Under the Constitution of India, as you have learnt in Chapter I, the legislative fields in entries 85 and 86 of the Union List in the Seventh Schedule specify Corporation tax and taxes on capital value of the assets, exclusive of agricultural land of individuals and companies. A tax on capital value of assets is a composite tax on the totality of all the assets owned by the company.

Article 366(6) of the Constitution defines corporate tax as follows:

Corporate tax means any tax on income, so far as that tax is payable by companies and is a tax in case the following conditions are fulfilled:

- (a) that it is not chargeable in respect of agricultural income;
- (b) that no deduction in respect of tax paid by companies is by any enactments which may apply to the tax authorised to be made from dividends payable by the companies to individuals;
- (c) that no provision exists for taking the tax so paid into account for computing for the purposes of Indian income tax, the total income of individuals receiving such dividends, or in computing the Indian income tax payable by, or refundable to, such individuals.

2.2 MEANING OF COMPANY UNDER SECTION 2(17) OF THE INCOME-TAX ACT

As per section 2(17), company means:

- (i) any Indian company, or

- (ii) any body corporate incorporated by or under the laws of a country outside India, or
- (iii) any institution, association or body which is or was assessable or was assessed as a company for any assessment year under the Indian Income Tax Act, 1922 (11 of 1922) or was assessed under this Act, as a company for any assessment year commencing on or before April 1, 1970; or
- (iv) any institution, association or body, whether incorporated or not and whether Indian or non-Indian, which is declared by general or special order of the CBDT to be a company.

Provided that such institution, association or body shall be deemed to be a company only for such assessment year or assessment years (whether commencing before the 1st day of April 1971, or on or after that date) as may be specified in the declaration.

CBDT Order

In cases where the Central Board for Direct Taxes (CBDT) specifies any association or body to be a company, it is essential that the order of the Board is taken to be valid only in respect of the assessment year or years specifically mentioned in the Board's order. The Board's power is specifically made exercisable in respect of past assessment year. In other words, the declaration of the Board does not automatically mean that the association or body would continue to be treated as a company for all purposes and for all assessment years. Whilst declaring any institution, association or body as a company, the Board has also to justify itself that they have characteristics as would generally enable them to be recognized as companies in common parlance as sometimes, such a declaration may be sought for by institutions for avoiding taxes.

The power of the Central Board of Direct Taxes to declare any foreign association or body as a company is absolute and unqualified and the Board would normally declare such association or body to be a 'company' only after taking into consideration the benefit to the revenue (Section 119 read together with Section 295 of the Income Tax Act, 1961).

Liquidating Company

A Company in liquidation is also a "company" and the Income tax authorities are entitled to call upon the liquidator to make a return of the company's income. Likewise, penalty proceedings can also be initiated against a company in liquidation for a default committed prior to liquidation. Thus, the expression Company as defined in the Income Tax Act has a much wider connotation than what is normally understood by a 'Company' under the Companies Act.

Companies established under section 25 of the Companies Act,1956

In order to be regarded as a taxable entity under the Income Tax Act, 1961, it is not essential that the company must always have a share capital and must have been formed with a profit motive. Even companies having no share capital and those, which are limited by guarantee, are assessable as companies for income-tax purposes even if such companies may have been formed without any profit motive and registered under Section 25 of the Companies Act 1956 (e.g. Chambers of Commerce etc.).

Under Section 28 (iii) of the Income tax Act, 1961, trade, professional or similar associations are liable to tax in respect of the income they derive from rendering of specific services to their members. Accordingly, in respect of specific services to their members, such entities, even if they are non-profit making, would become liable to tax under the Income tax Act as a company in respect of their income from business although they may not have been specifically formed to carry on any business with a view to make profit. A statutory corporation established under the Act of Parliament, Government companies and the State Government companies who carry on a trade or business would also be treated as a company for all purposes of income tax.

Discontinuance of Business

A company or for that matter, any assessee who discontinued their business are statutorily required to intimate to the Assessing Officer within 15 days (Section 176 of the Income Tax Act, 1961).

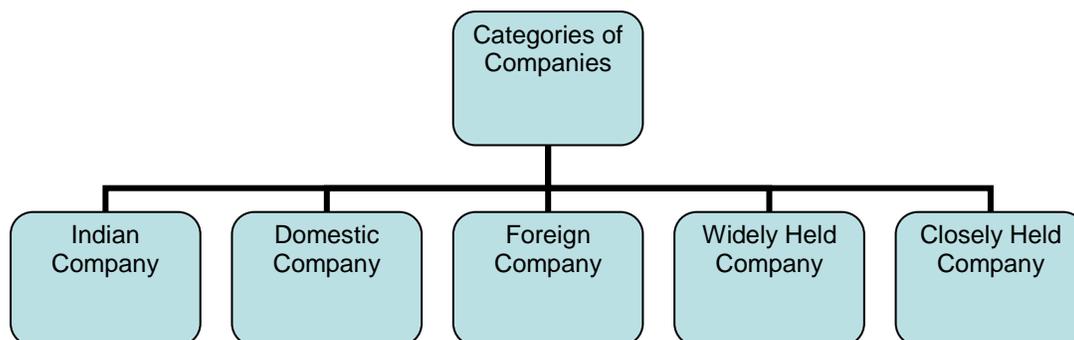
Assessment of Companies

For assessment to income tax, each company is assessed separately although the companies might be inter-related or inter-connected; for instance, holding and subsidiary companies must be assessed separately to Income tax in respect of the profits made by each of them since they have a separate and distinct legal existence.

*The Supreme Court in the case of Mrs. Bacha F. Guzdar v. CIT (1955) 27 ITR 1(SC) has held that **dividend** received from a company earning agricultural income is not an agricultural income in the hands of the shareholders and therefore **does not qualify for exemption** under Section 10 (1) which grants exemption to agricultural income.*

2.3 CATEGORIES OF COMPANIES UNDER THE INCOME TAX ACT, 1961

In continuation of our, earlier discussion on definition of company, we will now discuss broadly the different categories of companies:



Let us now discuss these in detail from taxation point of view.

2.3.1 Indian Company

Section 2(26) of the Income Tax Act, 1961 defines the expression 'Indian

Company' as a company formed and registered under the Companies Act, 1956 and includes:

- (a) a company formed and registered under any law relating to companies formerly in force in any part of India (other than the State of Jammu and Kashmir, and the Union Territories specified in (e) below);
- (b) any corporation established by or under a Central, State or Provincial Act;
- (c) any institution, association or body which is declared by the Board to be a company under Section 2(17) of the Income Tax Act, 1961;
- (d) in the case of State of Jammu & Kashmir, any company formed and registered under any law for the time being in force in that State; and
- (e) in the case of any of the Union Territories of Dadra and Nagar Haveli, Goa, Daman and Diu and Pondicherry, a company formed and registered under any law for the time being in force in that Union Territory;

Provided that the registered or, as the case may be, principal office of the company, corporation, institution, association or body in all cases is in India.

From the above definition, it may be seen that statutory corporations as well as government companies are automatically treated as Indian companies for purposes of the Income Tax Act, 1961. The definition of an Indian company has been specifically given under the Income Tax Act, 1961 because of the fact that Indian companies are entitled to certain special tax benefits under this Act. It must be noted that all companies falling within the definition given in Section 2(17) of the Act are not necessarily Indian companies whereas all Indian companies are companies within the meaning of Section 2(17) of the Act.

"Infrastructural capital company" as defined under Section 26A means such company which makes investments by way of acquiring shares or providing long-term finance to any enterprise or undertaking wholly engaged in the business referred to in Sub-section (4) of Section 90-IA or Sub-section (1) of Section 80-IAB or an undertaking developing and building a housing project referred to in Sub-section (10) of Section 80-IB or a project for constructing a hotel of not less than three-star category as classified by the Central Government or a project for constructing a hospital with at least one-hundred beds for patients.

2.3.2 Domestic Company

Section 2(22A) of the Income Tax Act, 1961, defines domestic company as an Indian company or any other company which, in respect of its income liable to tax under the Income Tax Act, has made the prescribed arrangements for the declaration and payment within India, of the dividends (including dividends on preference shares) payable out of such income.

From this definition, it is clear that all Indian companies are domestic companies while all domestic companies need not necessarily be Indian companies. In other words, a non-Indian company would be considered as a domestic company if it makes the prescribed arrangements for the declaration and payment of dividends in India on

which tax is deductible under Section 194. These arrangements are as follows:

- (i) the share register of the company concerned, for all its shareholders, shall be regularly maintained as its principal place of business within India in respect of any assessment year from a date not later than the first day of April of such year.
- (ii) the general meeting for passing the accounts of the previous year relevant to the assessment year declaring any dividends in respect thereof shall be held only at a place within India;
- (iii) the dividends declared, if any, shall be payable only within India to all shareholders.

2.3.3 Foreign Company

Section 2(23A) of the Income tax Act defines foreign company as a company, which, is not a domestic company. However, all non-Indian companies are not necessarily foreign companies. If a non-Indian company has made the prescribed arrangements for declaration and payments of dividends within India, such a non-Indian company must be treated as a “domestic company” and not as a “foreign company”.

Test Your Knowledge



A foreign company may be treated as domestic company under the Income Tax Act, 1961. True or False?

Answer: True, A foreign company shall become a domestic company if it has made arrangements for the declaration and payment of dividends in India which is payable out of domestic income.

2.3.4 COMPANY IN WHICH PUBLIC ARE SUBSTANTIALLY INTERESTED (A WIDELY-HELD COMPANY)

Section 2(18) of the Income Tax, Act defines the expression “company in which the public are substantially interested”.

A company is said to be one in which public are substantially interested in the following cases, namely –

- (i) If it is a company **owned by the Government or the Reserve Bank of India** or in which **not less than 40 per cent of the shares**, whether singly or taken together, are **held by the Government or the Reserve Bank of India** or a corporation owned by the Reserve Bank of India; or
- (ii) If it is a company which is **registered under Section 25 of the Companies Act, 1956**; or
- (iii) If it is a company, having no share capital and if, having regard to its objects,

the nature and composition of its membership and other relevant considerations, it is declared by an **order of the Board** (CBDT) to be a company in which the public are substantially interested. However, such a company shall be deemed to be one in which the public are substantially interested only for the assessment year(s) as may be specified in the declaration; or

- (iv) If it is a company which carries on, as its principal business, the business of acceptance of deposits from its members and which is declared by the Central Government under Section 620A of the Companies Act, 1956 to be a **Nidhi or Mutual Benefit Society**; or
- (v) If it is a company in which shares carrying **not less than 50 per cent** of the voting power have been allotted unconditionally to or acquired unconditionally by, and are throughout the relevant previous year beneficially held **by**, one or more **cooperative societies**; or
- (vi) If it is a company which is not a private company as defined in Section 3 of the Companies Act, 1956 and equity shares of the company (not being shares entitled to a fixed rate of dividend whether with or without a further right to participate in the profits, i.e. preference shares) were, as on the last day of the relevant previous year, **listed in a recognised stock** exchange in India;
- (vii) If it is a company which is not a private company within the meaning of the Companies Act, 1956, and the shares in the company (not being shares entitled to a fixed rate of dividend whether with or without a further right to participate in profits) **carrying not less than 50 per cent** (40 per cent in case of an industrial company) of the voting power have been allotted unconditionally to, or acquired unconditionally by, and were throughout the relevant accounting year beneficially held by (a) **the Government**, or (b) a corporation established by a Central or State or Provincial Act, or (c) any company in which the public are substantially interested or a wholly owned subsidiary company.

Industrial Company means an Indian company where business consists mainly in the construction of ships or in the manufacture or processing of goods or in mining or in the generation or distribution of electricity or any other form of power.

It may be noted that, a public company under the Companies Act, 1956 need not necessarily fall within the meaning of a company in which the public are substantially interested under the Income-tax Act, 1961 because a public company under the Companies Act, 1956 may be considered as one in which the public are not substantially interested under the Income-tax Act, 1961 after considering the nature and extent of shareholding.

2.3.5 Closely held company

A Company in which the public is not substantially interested is known as a closely-held company.

The distinction between a closely held and widely held company is significant from

the following viewpoints.

- (i) Section 2(22) (e), which deems certain payments as dividend, is applicable only to the shareholders of a closely-held company; and
- (ii) A closely held company is allowed to carry forward its business losses only if the conditions specified in Section 79 are satisfied.

2.4 TAX INCIDENCE UNDER INCOME TAX ACT, 1961

As you know the incidence of Income tax depends upon the residential status of a company in India during the relevant previous year. A Company may be either resident or non-resident in India, i.e., company can not be ordinary or non-ordinary residence.

According to Section 6(3) of the Act, a company is said to be resident in India (resident company) in any previous year, if:

- (i) It is an Indian company; or
- (ii) During that year, the control and management of its affairs is situated wholly in India.

If one of the above two tests is not satisfied the company would be a non-resident in India during that previous year.

According to Section 5(1) of the Act, the total income of a resident company would consist of:

- (i) income received or deemed to be received in India during the previous year by or on behalf of such company;
- (ii) income which accrues or arises or is deemed to accrue or arise to it in India during the previous year;
- (iii) income which accrues or arises to it outside India during the previous year.

It is important to note that under clause (iii) only income accruing or arising outside India is included. Income deemed to accrue or arise outside India is not includible in the hands of residents. Hence, net dividends received from foreign companies are includible in income and not the gross dividends [*CIT v. Shaw Wallace & Co. Ltd.* (1981) 132 ITR 466].

In this context, the Calcutta High Court had followed the Supreme Court's decision in *Commissioner of Income-tax v. Clive Insurance Co. Ltd.* (1978, 113 ITR 636) holding that the assessee could be said to have paid Income Tax in U.K, by deduction or otherwise, in respect of the net dividend so as to be eligible for relief contemplated by Section 49D of the Indian Income Tax Act, 1922. Following the Supreme Court's decision, the Bombay High Court held in the case of *Commissioner of Income tax v. Tata Chemicals Ltd.* (1986, 162 ITR 556) that the assessee was entitled to double taxation relief under Section 91 of the Income Tax Act, 1961 in respect of dividends from the United Kingdom. Following its decision in the case of *Shaw Wallace & Co. Ltd.* (supra), the Calcutta High Court held in the case of the same assessee (1983, 143 ITR 207) that dividends from foreign companies are to be assessed not on the gross amount of the dividends but on the gross amount of the dividends less tax deducted

there from in foreign countries. In other words, only the net foreign dividends are to be included in the total income of a resident assessee under Section 5(1)(c) of the Income Tax Act, 1961.

Under Section 5(2) of the Act, the total income of non-resident would consist of:

- (i) Income received or deemed to be received in India in the previous year by or on behalf of such company;
- (ii) Income which accrues or arises or is deemed to accrue or arise to it in India during the previous year.

The decision of the Supreme Court in the case of *Standard Triumph Motor Co. Ltd. v. CIT* (1993) 201 ITR 391 to the effect that when an Indian resident passes an entry crediting a non-resident with amount payable to him, that would tantamount to the latter receiving income in India, is pregnant with grave consequences. In this case, the royalty payable to non-resident in pound sterling was credited to the non-residents accounts in the books of the assessee. The Supreme Court held that the plea to accept royalty income in U.K. was immaterial because the amount was available for the use of the non-resident in India in any manner he liked. Hence, the income was received in India. In the wake of this decision, non-residents who have all along been held to be not liable to Indian Income-tax if the contract was signed outside India, executed outside India and paid for outside India could well fall into the Indian-tax net, should their clients/customers credit them for the amount due before making payments to them outside India. In other words, a non-resident's tax liability depends upon the accounting entry passed by his client customer.

2.5 RATES OF INCOME TAX FOR ASSESSMENT YEAR 2013-14

Domestic companies

For income other than long term capital gains	30% of total income plus surcharge @ 5%
On short term capital gains emanating from transfer of a short term capital asset being an equity share or unit of an equity oriented fund	15% plus surcharge @ 5%
On long-term capital gains emanating from transfer of a long term capital asset	20% plus surcharge @ 5%

Foreign companies

In the case of a company other than a domestic company—

On so much of the total income as consists of— royalties received from Government or an Indian concern in pursuance of an agreement made by it with the Government or the Indian concern after the 31st day of March, 1961 but before the 1st day of April, 1976; or fees for rendering technical services received from

Government or an Indian concern in pursuance of an agreement made by it with the Government or the Indian concern after the 29th day of February, 1964 but before the 1st day of April, 1976, and where such agreement has, in either case, been approved by the Central Government.

50% plus surcharge @2%.

On other incomes

40% plus surcharge @2%

- Note:** 1. Surcharge is applicable in case total income exceeds Rs. One Crore.
2. Plus Education Cess @ 2% and Secondary & Higher Education Cess @ 1% on tax & surcharge

2.6 MINIMUM ALTERNATE TAX (MAT)

Section 115J which was a special provision applicable to a company if its total income as computed under the Income tax Act was less than thirty per cent of its book profit was introduced with effect from 1.4.1988 but was discontinued with effect from 1.4.1991. It was revived as Section 115JA with effect from 1.4.1997 as a provision deeming total income equal to thirty per cent of book profit of companies referred to earlier. This provision was also discontinued with effect from 1.4.2001 but was substituted by Section 115JB effective from the same date. This provision follows concept of minimum alternate Tax.

As provided out in the Explanatory Memorandum to the Finance Bill, 2000, the Minimum Alternate Tax had been levied from the assessment year 1997-98 as the number of zero tax companies and companies paying marginal tax had proliferated. The efficacy of that provision, however, had declined in view of the exclusions of various sectors from the operation of MAT and the tax credit systems.

Hence, in its place the new provisions of Section 115JB were inserted which are simpler in application. They provide that all companies having book profits under the Companies Act shall have to pay a minimum alternate tax at a rate of 18.5% (as amended). These provisions are applicable to all corporate entities. According to this section, if the income tax payable by a company on its total income as computed under the Income Tax Act in respect of any previous year relevant to the assessment year commencing on or after the 1st day of April, 2012, is less than 18.5% of such book profit plus surcharge (Domestic Company = 18.5%+ surcharge @5% + education and Secondary & Higher Education Cess @ 3%) if applicable, the tax payable for the relevant previous year shall be deemed to be 18.5% of such book. This non-absolute provision will override any other provision of the Income Tax Act.

Sub-section (2) of this section requires the company in this case will prepare its profit and loss account for the relevant previous year in accordance with the provisions of Parts II of Schedule VI of the Companies Act, 1956. However, while preparing the annual accounts including profit and loss account —

- (a) the accounting policies;
- (b) the accounting standards followed for preparing such accounts including profit and loss accounts; and
- (c) the method and rates adopted for calculating the depreciation,

shall be the same as have been adopted for the purpose of preparing such accounts including profit and loss account and laid before the company at its annual general meeting in accordance with the provisions of Section 210 of the Companies Act, 1956. But where the company has adopted or adopts the financial year, which is different from the previous year under the Income Tax Act, (a), (b) and (c) aforesaid shall correspond to the accounting policies, accounting standards and the method and rates for calculating the depreciation which have been adopted for preparing such accounts including profit and loss account for such financial year or part of such financial year falling within the relevant previous year.

As per section 115JB, every company is required to prepare its accounts as per Schedule VI of the Companies Act, 1956. However, as per the provisions of the Companies Act, 1956, certain companies, e.g. Insurance, Banking or Electricity Company, are allowed to prepare their profit and loss account in accordance with the provisions specified in their regulatory Acts.

In order to align the provisions of Income-tax Act with the Companies Act, 1956, with effect from assessment year 2013-14, section 115JB has been amended to provide that the companies which are not required under section 211 of the Companies Act to prepare their profit and loss account in accordance with the Schedule VI of the Companies Act, 1956, profit and loss account prepared in accordance with the provisions of their regulatory Acts shall be taken as a basis for computing the book profit under section 115JB.

However, a sub-section (5A) has been inserted to section 5, w.r.e.f A.Y. 2001-02, which provides that the MAT provisions shall not apply to any income accruing or arising to a company from life insurance business.

2.6.1 Meaning of “Book Profit”

As per Explanation below Sub-section (2), “Book Profit” means the net profit as shown in the profit and loss account for the relevant previous year prepared under this sub-section as increased by the following amounts:

- (a) the amount of Income tax paid or payable, and the provision therefor; or
- (b) the amounts carried to any reserves, by whatever name called other than reserve specified under Section 33AC, i.e, shipping reserve; or
- (c) the amount or amounts set aside to provisions made for meeting liabilities, other than ascertained liabilities, i.e. unascertained liabilities; or
- (d) the amount by way of provision for losses of subsidiary companies; or
- (e) in the amount or amounts of dividends paid or proposed; or
- (f) the amount or amounts of expenditure relatable to any income to which Section 10 other than the provisions contained in Clause (23G) and clause 38 from the assessment year 2007-08 thereof or Section 11 or Section 12 apply.
- (g) the amount of depreciation.
- (h) the amount of deferred tax and provisions therefore (inserted by Finance Act, 2008 with retrospective effect from 1.4.2001).

- (i) the amount or amounts set aside as provision for diminution in the value of any asset (w.r.e.f. 1.4.2001)
- (j) the amount standing in revaluation reserve relating to revalued asset on the retirement or disposal of such asset.

If any of the above amount referred in clauses (a) to (i) is debited to the profit and loss account or if any amount referred in clause (j) is not credited to the profit and loss account shall be added back to the net profit.

The net profit as increased by the amounts referred to in Clauses (a) to (j) shall be reduced by the following amounts:

- (i) the amount withdrawn from any reserves or provisions if any such amount is credited to the profit and loss account;

Provided that, where this section is applicable to an assessee in any previous year, the amount withdrawn from reserves created or provisions made in a previous year relevant to the assessment year commencing on or after the 1st day of April, 1997 shall not be reduced from the book profit unless the book profit of such year has been increased by those reserves or provisions (out of which the said amount was withdrawn) under this Explanation or Explanation below second proviso to Section 115JA, as the case may be; or
- (ii) the amount of income to which any of the provisions of Section 10 or Section 11 or Section 12 apply, if any such amount is credited to the profit and loss account; or
- (iia) the amount of depreciation debited to the profit and loss account (excluding the depreciation on account of revaluation of assets); or
- (iib) the amount withdrawn from revaluation reserve and credited to the profit and loss account, to the extent it does not exceed the amount of depreciation on account of revaluation of assets referred to in Clause (iia); or
- (iii) the amount of loss brought forward or unabsorbed depreciation, whichever is less, as per books of account. For the purposes of this clause, the loss shall not include depreciation. Therefore, in a case where an assessee has shown profit in a year, but after adjustment of depreciation it results profit or loss, no adjustment in book profit is allowed; or
- (iv) the amount of profits of sick industrial company for the assessment year commencing on and from the assessment year relevant to the previous year in which the said company has become a sick industrial company under Sub-section (1) of Section 17 of the Sick Industrial Companies (Special Provisions) Act, 1985 and ending with the assessment year during which the entire net worth of such company becomes equal to or exceeds the accumulated losses. "Net Worth" shall have the meaning assigned to it in Clause (ga) of Sub-section (1) of Section 3 of the Sick Industrial Companies (Special Provisions) Act, 1985.
- (v) The amount of deferred tax, if any such amount is credited to the profit and loss account.

The following points should also be noted in this context:

1. Nothing contained in Sub-section (1) shall affect the determination of the amounts unabsorbed depreciation under Section 32(2), business loss u/s 72(1), speculation loss u/s 73, capital loss u/s 74 and loss u/s 74A in relation to the relevant previous year to be carried forward to the subsequent year or years.
2. Every company to which this section applies, shall furnish a report in the prescribed form from an accountant as defined in the Explanation below Sub-section (2) of Section 288, certifying that the book profit has been computed in accordance with the provisions of this section along with the return of income filed under Sub-section (1) of Section 139 or along with the return of income furnished in response to a notice under Clause (I) of Sub-section (1) of Section 142.
3. Save as otherwise provided in this section, all other provisions of this Act shall apply to every assessee, being a company, mentioned in this section.
4. The provisions of this Section shall apply to the income accrued or arising on or after the 1st day of April, 2005 from any business carried on, or services rendered, by an entrepreneur or a Developer, in a Unit or Special Economic Zone, as the case may be (amendment made by Finance Act, 2011 and shall be effective from Assessment Year 2012-13, earlier the MAT provisions does not apply to SEZ enterprises and SEZ developers).

Whether the provisions of MAT applicable to foreign companies or not?

The Authority for Advance Ruling ("AAR") has delivered a ruling in the case of Timken India Ltd. In re (2005) 273 ITR 67 (AAR) where it holds that the provisions of section 115JB of the Income-tax Act, 1961 ("the Act") levying Minimum Alternate Tax ("MAT") on the book profit of a Company would not apply to a Foreign Company not having any physical presence in India. In this case, the AAR distinguished its earlier ruling of 1998 (234 ITR 828) wherein it had held that a foreign company would be subject to MAT provisions. The critical factor for distinguishing was on the basis that in the earlier ruling the applicant had a project office in India, which constituted a Permanent Establishment and was preparing its financial statements as required under Indian Companies Act, 1956. In order to comply with the requirement of MAT provisions regarding preparing Profit & Loss Account in accordance with the provisions of the Indian Companies Act, it is essential that the foreign company should have a place of business within India.

2.6.2 MAT Credit

Credit of MAT paid under the new provision of Section 115JB is available. However, the credit for the brought forward MAT paid under the old provisions of Section 115JA is allowed against the regular tax payable. It may be noted that the tax credit facility was available upto the assessment year 2000-2001 from the assessment year 1997-98. It could be carried forward for 5 assessment years. Thus, only carried forward balance may be set off during the remaining period of 5 years. From assessment year 2006-07, credit of MAT in respect of excess paid under Section 115JB will be available and it can be carried forward for 10 assessment years (prior to

assessment year 2010-11 it could be carried forward for 7 assessment year only, amended by Finance Act, 2009).

It is available to a company assessee. From assessment year 2012-13, if the income-tax payable is less than 18.5% of Book profit, then such book profit will be deemed to be the total income and income-tax will be payable @18.5% on such Book profit. Such company assessee has to prepare Profit & Loss A/c in accordance with the provisions of Part I and II of Schedule VI of the Companies Act, 1956.

2.7 Dividend Distribution Tax U/s 115O

A domestic company is liable to pay tax on the amounts distributed, declared or paid as dividend (whether interim or otherwise), it shall be payable @15% plus surcharge @5% and education cess & SHEC @3% in addition to the income tax payable.

The amount distributed, declared or paid as dividend may be out of accumulated or current year profits and the same shall exclude:

- (i) the amount of dividend received by the domestic company during the financial year, if
 - (a) such dividend is received from its subsidiary; and
 - (b) the subsidiary has paid the tax which is payable under this section on such dividend.
- (ii) the amount of dividend paid to any person for, or on behalf of, the New Pension System Trust referred to in clause (44) of Section 10.

The word dividend shall not include deemed dividend u/s 2(22)(e) i.e. loan or advance given by a closely held company to a substantial shareholder but include dividend u/s 2(22)(a), (b), (c) & (d).

Finance Act, 2011 insert a proviso to sub-section 6 of section 115O by which the provisions of section 115O shall also be applicable on an enterprise or undertaking engaged in developing, operating and maintaining a SEZ. The amount of such tax shall be deposited within 14 days from the date of:

- (a) declaration of dividend or
- (b) distribution of dividend or
- (c) payment of dividend

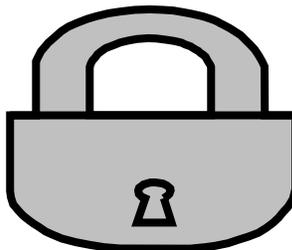
Whichever is earliest.

Taxation of Foreign Dividends (Section 115BBD):

Finance Act, 2011 insert a new section 115BBD for taxing foreign dividends received from a foreign company (in which the Indian Company holds 26% or more of equity share capital) at the rate of 15% plus surcharge @5% and education cess & SHEC @3%. No expenditure in respect of such dividends shall be allowed under the Act.

LESSON ROUND UP

- Article 366(6) of the Constitution defines corporate tax.
- As per section 2(17) of the Income Tax Act, Company means any Indian Company, or any body corporate incorporated by or under the laws of a country outside India, or any institution, association or body which is or was assessable or was assessed as a company for any assessment year under the Indian Income Tax Act, 1922 (11 of 1922) or was assessed under this Act, as a company for any assessment year commencing on or before April 1, 1970; or any institution, association or body, whether incorporated or not and whether Indian or non-Indian, which is declared by general or special order of the CBDT to be a company.
- Broadly speaking, Companies under the Income Tax Act are companies in which the public are substantially interested also referred to as widely-held companies and companies in which public are not substantially interested and also referred to as closely held company.
- Minimum Alternate Tax ("MAT") on the book profit of a Company would not apply to a Foreign Company not having any physical presence in India.
- A domestic company is liable to pay tax on the amounts distributed, declared or paid as dividend (whether interim or otherwise), it shall be payable @ 15% plus surcharge @5% and education cess and SHEC @3% in addition to the income tax payable.
- Section 115BBD provides for taxing foreign dividends received from a foreign company at the rate of 15% plus surcharge @5% and education cess and SHEC @ 3%.

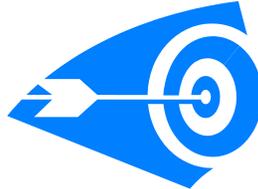
SELF-TEST QUESTIONS

1. Define the following keeping in view the points involved while planning tax:
 - (a) Indian Company
 - (b) Domestic Company
 - (c) Foreign Company
 - (d) Company in which public is substantially interested.
 - (e) Closely-held Company.

2. Explain the significance of classification of companies under the Income tax Act, 1961 and their impact on the tax liability.
 3. Explain how is the residential status of a company determined under the Income tax Act, 1961.
 4. Explain how (i) the scope of tax liability on total income and, (ii) the rate of the tax applicable to a company are determined?
 5. Explain the concept of MAT and its rationale.
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STUDY III
TAX PLANNING

LEARNING OBJECTIVES



The objective of the study lesson is to enable the students to understand:

- Concept of Tax Planning
- Right To Plan Tax Liability
- Tax Planning, Tax Evasion And Tax Avoidance
- Objectives of Tax Planning
- Importance of Tax Planning
- Essentials of Tax Planning
- Types of Tax Planning
- Areas of Tax Planning in the Context of Income Tax Act, 1961
 - Form of organization/ownership pattern
 - Locational Aspects
 - Nature of business
 - Tax planning in respect of corporate restructuring
 - Tax planning in respect of financial management
 - Tax planning in respect of employees remunerations
 - Tax planning in respect of specific managerial decisions
 - Tax planning in respect of Non-Residents
- Planning in the Context of Court Rulings and Legislative Amendments
- Statutory Force of the Notifications
- Organisation of tax planning cells
- Overall tax planning measures
- Some general considerations regarding new business
- Setting up and commencement of business *vis a vis* tax planning

3.1 CONCEPT OF TAX PLANNING

Tax Planning is an exercise undertaken to minimize tax liability through the best use of all available allowances, deductions, exclusions, exemptions, etc., to reduce income and/or capital gains.

Tax planning can be defined as an arrangement of one's financial and business affairs by taking legitimately in full benefit of all deductions, exemptions, allowances and rebates so that tax liability reduces to minimum. In other words, all arrangements by which the tax is saved by ways and means which comply with the legal obligations and requirements and are not colourable devices or tactics to meet the letters of law but not the spirit behind these, would constitute tax planning.

The Hon'ble Supreme Court in McDowell & Co. v. CTO (1985) 154 ITR 148 has observed that "tax planning may be legitimate provided it is within the framework of the law. Colourable devices cannot be part of tax planning and it is wrong to encourage or entertain the belief that it is honourable to avoid payment of tax by resorting to dubious methods." Tax planning should not be done with intent to defraud the revenue; though all transactions entered into by an assessee could be legally correct, yet on the whole these transactions may be devised to defraud the revenue. All such devices where statute is followed in strict words but actually spirit behind the statute is marred would be termed as colourable devices and they do not form part of tax planning. All transactions in respect of tax planning must to be in accordance with the true spirit of statute and should be correct in form and substance.

Various judicial pronouncements have laid down the principle that substance and form of the transactions shall be seen in totality to determine the net effect of a particular transaction. The Hon'ble Supreme Court in the case of *CIT v. B M Kharwar* (1969) 72 ITR 603 has held that, " The taxing authority is entitled and is indeed bound to determine the true legal relation resulting from a transaction. If the parties have chosen to conceal by a device the legal relation, it is open to the taxing authorities to unravel the device and to determine the true character of relationship. But the legal effect of a transaction can not be displaced by a probing into substance of the transaction."

The form and substance of a transaction is real test of any tax-planning device. The form of transaction refers to transaction, as it appears superficially and the real intention behind such transaction may remain concealed. Substance of a transaction refers to lifting the veil of legal documents and ascertaining the true intention of parties behind the transaction.

How Tax is levied

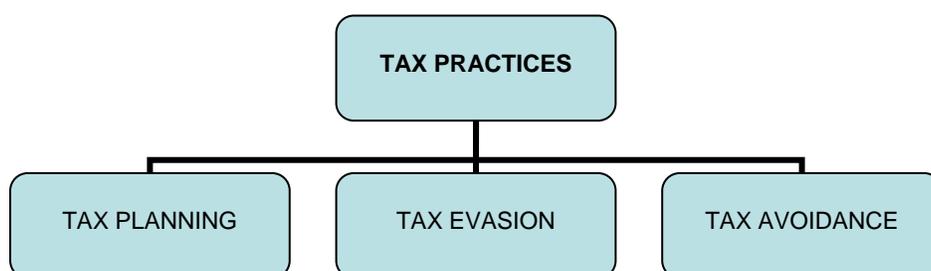
Before a discussion is made concerning the concept of tax planning in detail it needs to be understood as to how tax is levied.

Liability of tax depends upon the ***charging section in the statute vis-a-vis 'taxable person', 'taxable event' and 'subject matter of taxation'***. For understanding these inter-related but distinct concepts reference may be made to the Supreme Court's decision in *State of Tamil Nadu v. M.K. Kandaswami* (1975, 36 STC 191). No tax is complete nor a charge can rise under a fiscal statute unless the subject, the object and the quantum of tax are prescribed or indicated in the provision. In doing so, there can be different rates of tax levied upon the nature of business/profession carried on or depending on the capacity of the person to pay the tax and/or other relevant consideration. It is now well settled that a modern State, particularly when exercising powers of taxation, has to deal with complex factors/relating to the objects to be taxed, tax to be levied, the social and economic policies etc. Though wide latitude is given to the legislature in the matter of levy of taxes, what is needed is that the tax/statute should be constitutionally valid to pass the muster of Article 14 of the Constitution of India. Article 265 of the Constitution of India prescribes that "no tax shall be levied or collected except by authority".

No income should be taxed presumptively. There is no equity about taxation and no income should be taxed twice.

3.2 TAX PLANNING, TAX AVOIDANCE AND TAX EVASION

In India the tax laws are admittedly complicated because of various deductions, exemptions, relief and rebates. Therefore, it is only logical that taxpayers generally plan their affairs so as to attract the least incidence of tax. However, practice of avoidance is worldwide phenomenon and there is always a continuing battle in this regard between the taxpayer and the tax collector. The perceptions of both are different. The taxpayer spares no efforts in maximising his profits and attracting the least incidence. The tax gatherer, on the other hand, tries to break the plans whose sole objective is to save taxes.



In the context of saving tax, there are three commonly used practices, namely (a) Tax Evasion; (b) Tax Avoidance; (c) Tax Planning. They are being considered in greater details in subsequent discussion.

- (a) **Tax Evasion:** It refers to a situation where a person tries to reduce his tax liability by deliberately suppressing the income or by inflating the expenditure showing the income lower than the actual income and resorting to various types of deliberate manipulations. An assessee guilty of tax evasion is punishable under the relevant laws. Tax evasion may involve stating an untrue statement knowingly, submitting misleading documents, suppression of facts, not maintaining proper accounts of income earned (if required under the law) omission of material facts in assessments. An assessee who dishonestly claims the benefit under the statute by making false statements, would be guilty of tax evasion.
- (b) **Tax Avoidance :** The line of demarcation between tax planning and tax avoidance is very thin and blurred. There could be elements of malafide motive involved in tax avoidance also. Any planning which, though done strictly according to legal requirements defeats the basic intention of the Legislature behind the statute could be termed as instance of tax avoidance. It is usually done by adjusting the affairs in such a manner that there is no infringement of taxation laws and by taking full advantage of the loopholes therein so as to attract the least incidence of tax. Earlier tax avoidance was considered completely legitimate, but at present it may be illegitimate in certain situations. In the latest judgement of the Supreme Court in McDowell's case 1985 (154 ITR 148) SC, tax avoidance has been considered as heinous as tax evasion and a crime against society. Most of the amendments are now aimed at curbing practice of avoidance.

(c) **Tax Planning:** It means arranging the financial activities in such a way that maximum tax benefits are enjoyed by making use of all beneficial provisions in the tax laws which entitle the assessee to get certain rebates and reliefs. This is permitted and not frowned upon by law. Thus, tax planning would imply compliance with the taxation provisions in such a manner that full advantage is taken of all tax exemptions, deductions, concessions, rebates and reliefs permissible under the Income Tax Act so that the incidence of tax is the least. Tax planning can neither be equated to tax evasion nor to tax avoidance with reference to a company, it is the scientific planning of the company's operations in such a way so as to attract minimum liability to tax or postponement or for that matter deferment of the tax liability for the subsequent period by availing various incentives, concessions, allowances, rebates and reliefs provided for in the tax laws. They are meant to be availed of and they have certain clear objectives to achieve. Tax planning may, therefore, be regarded as a method of intelligent application of expert knowledge of planning corporate affairs with a view to securing consciously provided tax benefits on the basis of the national priorities in consonance with the interests of the State and the public.

You have learnt that *tax planning implies the reduction of tax liability with full compliance of tax laws and meeting the tax obligations*, which though technically satisfying the requirements of law, do not represent the legislative intention on the basis of national priorities.

The types of cases that come under '**Tax avoidance**' are those where the tax payer has apparently circumvented the law, without giving rise to an offence, by the use of a scheme, arrangement or device though of a complex nature, whose main or sole purpose is to defer, reduce or completely avoid the tax payable under the law. Sometimes, the avoidance is accomplished by shifting the liability for tax to other person not at arm's length in whose hands the tax payable is reduced or eliminated. According to G.S.A. Wheat Craft, "tax avoidance is the act of dodging tax without actually breaking the law". It is a method of reducing incidence of tax by taking advantages of certain loopholes of tax laws. Thus, the line of demarcation between tax avoidance and tax planning is very thin and blurred. There is an element of malafide motive involved in tax avoidance.

The Royal Commission on Taxation for Canada has explained the concept of tax avoidance as under :

For our purposes.....the expression "Tax Avoidance" will be used to describe every attempt by legal means to prevent or reduce tax liability which would otherwise be incurred, by taking advantage of some provisions or lack of provisions of law. It excludes fraud, concealment or other illegal measures".

Tax evasion is a method of evading tax liability by dishonest means like suppression, showing lower incomes, conscious violation of rules, inflation of expenses etc. This device has to be condemned. It is a dubious way of attempting to get tax gains. A tax evader has to pay not only penalty but he also incurs the risk of being prosecuted. Tax evasion can never be construed as tax planning because it amounts to breaking of law whereas tax planning is devised within the legal

framework by availing of what the legislature provides. Tax planning ensures not only accrual of tax benefits within the four corners of law but it also ensures that tax obligations are properly discharged so as to avoid penal provisions.

3.3 OBJECTIVES OF TAX PLANNING

Tax planning, in fact, is an honest and rightful approach to the attainment of maximum benefits of the taxation laws within their framework. Therefore, the objectives of tax planning cannot be regarded as offending any concept of the taxation laws and subjected to reprehension of reducing the inflow of revenue to the Government's coffers, so long as the tax planning measures are in conformity with the statute laws and the judicial expositions thereof. The basic objectives of tax planning are:

- (a) Reduction of tax liability
- (b) Minimisation of litigation
- (c) Productive investment
- (d) Healthy growth of economy
- (e) Economic stability

(a) Reduction of tax liability: In this context, a tax payer can derive the maximum savings by arranging his affairs in accordance with the requirements of law, as contained in the fiscal statutes. In many a cases, a taxpayer may suffer heavy taxation not on account of the dosage of tax administered by the Act, but, because of his lack of awareness of the legal requirements. Since every taxpayer wishes to retain a maximum part of his earnings, rather than parting with it and facing the resource crunch, it would be to his benefit to plan his tax affairs properly and avail the deductions and exemption admissible under the Act (s). He can succeed in doing so by keeping an awareness of the implications of the various business/other transactions as well as updation of his knowledge about the various concessions for which he is eligible.

(b) Minimisation of litigation: A general visualisation of the tax administration scenario depicts a tug-of-war the tax payers trying their maximum to pay the least tax and the tax administrator attempting to extract the maximum. This also results in, sometimes, protracted litigations. It is in this context that a sound tax planning pays dividends. Where a proper tax planning is adopted by the tax payer in conformity with the provisions of the taxation laws, the incidence of litigation is minimised. This saves him from the hardships and inconveniences caused by the unnecessary litigations, which at times even stretch upto the High/Supreme Court levels':

(c) Productive Investment: Channelisation, by a tax payer, of his otherwise taxable income to the various investment schemes too is one of the prime objectives of tax planning as it is aimed to attain twin-objectives : (i) to harness the resources for socially productive projects, and, (ii) to relieve the tax payer not only from the initial brunt of taxation, but also to convert the earnings so made into means of further earnings. Legal awareness of the avenues so provided by the Government, from time to time, negates the imperative avoidance/evasion and lend authenticity to the investments made.

(d) Healthy Growth of Economy: The growth of a nation's economy is

synonymous with the growth and prosperity of its citizens. In this context, a saving of earnings by legally sanctioned devices fosters the growth of both, because savings by dubious means lead to generation of black money, the evils of which are obvious. Conversely, tax-planning measures are aimed at generating white money having a free flow and generation without reservations for the overall progress of the nation. Tax planning assumes a great significance in this context.

(e) Economic Stability: In the context of the case, *M.V. Valliapan v. ITO*, (1988) 170 ITR 238 (Mad.), by a proper tax planning, a smooth tax flow from the tax payer to the tax administrator, without recriminations, is ensured. This results in economic stability by way of: (i) availing of avenues for productive investments by the tax payers and, (ii) harnessing of resources for national projects aimed at general prosperity of the national economy and reaping of benefits even by those not liable to pay tax on their incomes. Therefore, notwithstanding the legal rulings in cases like *McDowell* and its English parallels, real and genuine transactions aimed at a valid tax planning cannot be turned down merely on grounds of reduction of the tax burden.

While planning a scheme relating to tax affairs, what needs to be assured is that tax planning device does not lose its efficiency due to changes in law. It would be a shortsighted perspective to think of a planning device that is in conformity with the law as it exists, but gets nullified by a subsequent change in law specially where the change is of a retrospective nature. Hence, the tax plan has to be flexible in nature. Flexibility has to be considered as a practical feature in a tax system. Hence, a planner has to comprehend about the future scenario too while devising a plan to save tax.

In the context of corporate taxation since the incidence of tax on Indian companies is considered quite high the scope for ploughing back of profits for expansion and modernisation of the existing plant and machinery etc. is considerably narrowed down. Thus the company has to plan its taxation in such a way that will enable it to avail the tax incentives etc. provided by the Government to the maximum.

3.4 IMPORTANCE OF TAX PLANNING

We cannot deny the fact that tax planning is important for reducing the tax liability. It is also considered important on account of the following factors :

- (i) When an assessee has not claimed all the deductions and relief, before the assessment is completed, he is not allowed to claim them at that the time of appeal. It was held in *CIT v. Gurjargravures Ltd.* (1972) 84 ITR 723 that if there is no tax planning and there are lapses on the part of the assessee, the benefit would be the least.
- (ii) Tax planning exercise is more reliable since the Companies Act, 1956 and other allied laws narrow down the scope for tax evasion and tax avoidance techniques, driving a taxpayer to a situation where he will be subjected to severe penal consequences.
- (iii) Presently, companies are supposed to promote those activities and programmes, which are of public interest and good for a civilised society. In

order to encourage these, the Government has provided them with incentives in the tax laws. Hence a planner has to be well versed with the law concerning incentives.

- (iv) With increase in profits, the quantum of corporate tax also increases and it necessitates the devotion of adequate time on tax planning.
- (v) Tax planning enables a company to bear the burden of both direct and indirect taxation during inflation. It enables companies to make proper expense planning, capital budget planning, sales promotion planning etc.
- (vi) Repairs, renewals, modernisation and replacement of plant and machinery are indispensable for an industry for its continuous growth. The need for capital formation in the corporate sector cannot be ignored and heavy taxation reduces the inflow of corporate funds. Capital formation helps in replacing the technologically obsolete and outdated plant and machinery and enables the carrying on of manufacturing operation with a new and more sophisticated system. Any decision of this kind would involve huge capital expenditure which is financed generally by ploughing back the profits, utilisation of reserves and surplus along with the availing of deductions are revenue expenditure incurred for undertaking modernisation, replacement, repairs and renewal of plant and machinery etc. Availability of accumulated profits, reserves and surpluses and claiming such expenses as revenue expenditure are possible through proper implementation of tax planning techniques.
- (vii) In these days of credit squeeze and dear money conditions, even a rupee of tax decently saved may be taken as an interest-free loan from the Government, which perhaps, an assessee need not repay.

Thus, any legitimate step taken by an assessee (being a company) directed towards maximising tax benefits, keeping in view the intention of law, will not only help it but also the society since it promotes the spirit behind the legal provisions. All those companies which practice tax planning may have the satisfaction that they are contributing their best to the nation's broad objectives and goals in a welfare State like ours. At the same time, the law makes the fulfillment of certain conditions obligatory before allowing the benefits to be claimed by the companies. In this way, the companies, besides helping themselves, also help in securing the objectives, tasks and goals set before them by the country.

3.5 Diversion of Income and Application of Income

The Supreme Court's verdict in *CIT v. Sitaldas Tirthdas* (1961) 41 ITR 367 is the authority for the proposition that where by an obligation income is diverted before it reaches the assessee, it is deductible from his income as for all practical purposes it is not his income at all but where the income is required to be applied to discharge an obligation after it reaches the assessee, it is not deductible. Thus, there is the difference between diversion of income by an overriding title and application of income as the former is deductible while the latter is not. Thus, when management of a company is taken over by another person from the existing team in consideration of percentage of future profits to the latter, in computing the business income of the

former, such percentage of profits is deductible [*CIT v. Travancore Sugars and Chemicals Ltd.* (1973) 88 ITR 1 (SC)]. Management agreements must therefore be drafted with caution.

The Delhi High Court's verdict in *CIT v. Stellar Investments Ltd.* (1991) 192 ITR 287 to the effect that the Assessing Officer in terms of the power available to him under Section 68 of the Act, is not precluded from ascertaining the genuineness of the share capital, must be heeded. There have been occasions when unscrupulous promoters have ploughed back their black money into new companies by subscribing to shares in thousands of fictitious names. If the bluff is called, the unexplained credit in the form of share capital would be treated as income under Section 68 of the Act.

3.6 ESSENTIALS OF TAX PLANNING

Successful tax planning techniques should have following attributes :

- (a) It should be based on upto date knowledge of tax laws. Not only is an upto date knowledge of the statute law necessary, assessee must also be aware of judgments made through various decisions of the courts. In addition, one must keep track of the circulars, notifications, clarifications and Administrative instructions issued by the CBDT from time to time.
- (b) The disclosure of all material information and furnishing the same to the income-tax department is an absolute pre-requisite of tax planning as concealment in any form would attract the penalty clauses – the penalty often ranging from 100 to 300% of the amount of tax sought to be evaded. Section 271(1)(c) read together with explanations there to.
- (c) Whatever is planned should not simply satisfy the requirements of law by complying with legal provisions as stated and meeting the tax obligations but also should be within the framework of law. It means that sham transactions or make-believe transactions or colourable devices, which are entered into just with a view to circumvent the legal provisions, must be avoided.

Every citizen is obliged to honestly pay the taxes. Therefore, only colourable devices resorted to by the tax payers for evading a tax liability will have to be ignored by the court. Accordingly, a tax planning within the four corners of the taxation laws is not to be turned down only because it legitimately reduces the tax inflow to the Government. A genuine tax-planning device, aimed at carrying out the rules of law and courts' decisions and to overcome heavy burden of taxation, if fully valid.

- (d) A planning model must be capable of attainment of the desired objectives of a business and be amenable to its possible future changes. Therefore, all the important areas of corporate planning, whether related to strategic planning, project planning or operational planning involving tax considerations for long-term or short-term management objectives and policies should be strictly scrutinised in relative situations. Foresight is the essence of a business. Tax planning is one of its important attributes.

3.7 TYPES OF TAX PLANNING

The tax planning exercise ranges from devising a model for specific transaction

as well as for systematic corporate planning. These are:

- (a) Short-range and long-range tax planning.
- (b) Permissive tax planning.
- (c) Purposive tax planning.

(a) Short-range planning refers to year to year planning to achieve some specific or limited objective. For example, an individual assessee whose income is likely to register unusual growth in particular year as compared to the preceding year, may plan to subscribe to the PPF/NSC's within the prescribed limits in order to enjoy substantive tax relief. By investing in such a way, he is not making permanent commitment but is substantially saving in the tax. It is one of the examples of short-range planning.

Long-range planning on the other hand, involves entering into activities, which may not pay-off immediately. For example, when an assessee transfers his equity shares to his minor son he knows that the Income from the shares will be clubbed with his own income. But clubbing would also cease after minor attains majority.

(b) Permissive tax planning is tax planning under the express provisions of tax laws. Tax laws of our country offer many exemptions and incentives.

(c) Purposive tax planning is based on the measures which circumvent the law. The permissive tax planning has the express sanction of the Statute while the purposive tax planning does not carry such sanction. For example, under Sections 60 to 65 of the Income-tax Act, 1961 the income of the other persons is clubbed in the income of the assessee. If the assessee is in a position to plan in such a way that these provisions do not get attracted, Such a plan would work in favour of the tax payer because it would increase his disposable resources. Such a tax plan could be termed as 'Purposive Tax Planning'.

3.8 AREAS OF TAX PLANNING IN THE CONTEXT OF INCOME TAX ACT, 1961

Some of the important areas where planning can be attempted in an organised manner are as under:

- (a) Form of organisation/ownership pattern;
- (b) Locational aspects;
- (c) Nature of business.
- (d) Tax planning in respect of corporate restructuring;
- (e) Tax planning in respect of financial management;
- (f) Tax planning in respect of employees remunerations;
- (g) Tax planning in respect of specific managerial decisions;
- (h) Tax planning in respect of Non-Residents.

3.8.1 FORM OF THE ORGANISATION

We have indicated above some of the important areas where tax planning can be attempted. In this study we shall discuss the first aspect of setting up of new

business entity, namely form of organisation/ownership pattern. The selection of particular form of organisation depends not only on the magnitude of financial requirements and owner's liability, but also on the tax considerations. In the case of a company, the law interferes with the corporate planning process from the moment it comes into existence. At times, tax laws affect even the periods prior to the existence of a company and it can also extend upto the point of time when the company ceases to exist. For example, a director of a private limited company in liquidation, has to keep in view the provisions of Sections 178 and 179 of the Income Tax Act, 1961 dealing with misfeasance etc. Normally, depending upon the level of operation, expected profitability need for external financing and expected requirements of technical expertise, a suitable form can be chosen. But in view of the continuity of business, the benefits arising out of limited liability, organised accounting and the overall long-term tax benefits flowing to the company form of organisation, the corporate enterprise may be regarded as an effective instrument of tax planning. The company being a separate legal entity, confers certain valuable benefits in the matter of tax planning to its shareholders and the persons connected with the management of the company.

(A) Company Form of Organisation

The important tax privileges and advantages to a company over the other forms can be summarized as under:

- (i) **Allowability of remuneration**, for the persons who are managing the affairs of the company and also owning its shares.
- (ii) The provisions relating to **clubbing of income under Section 64** of the Income Tax Act, 1961 do not apply even if the business is carried on by family members through a company, which ultimately leads to reduction in liability to tax on the part of the individual members. However, if spouse of an individual having a substantial interest in a company receives remuneration from the same company, such remuneration is added to the income of the individual unless the spouse is technically or professionally qualified. [Section 40A(2)(b) of the Income Tax Act, 1961].
- (iii) Any income by way of dividend referred to in Section 115-O is **exempt** under Section 10(34).
- (iv) **Companies are subjected to flat rate of tax**, regardless of the quantum of their income. The domestic companies now pay tax @ 30% plus surcharge @ 5%, if applicable and education cess @ 3%.. This, however, may not seem to be an advantage in view of low slab rates applicable to sole proprietorships, but when we look at the total incidence of tax after taking into account the various deductions allowed to companies and the scheme of perquisites, the real owners of companies to stand to benefit.
- (v) There are certain **special tax concessions**, allowances and deductions given under the Income Tax Act, 1961 **available only to the company** form of business enterprises such as deductions allowed under Section 33AC and Sections 36(1)(ix) and 35D of the Income Tax Act, 1961 etc.

- (vi) Incorporation of a company has the incidental advantage of attracting large capital since the shareholder, who has to contribute only a miniscule part of the capital requirements, is assured of limited liability and free transferability of his shares. That shares in companies are treated as long term capital assets qualifying for considerable leniency in taxation even if they are held by the assessee for a small time as 12 months, has made investment in the shares of companies all the more attractive. This helps the companies to generate the funds required for their development as well as furtherance of their objects.
- (vii) There is **no wealth tax on shares of company** w. e. f. Assessment Year 1993-94. In case there is every likelihood of growth of business in future years a partnership firm or sole proprietorship business may be formed initially and may be converted into a company later, on growth of business as the average rate of tax applicable for non-corporate assessee is less than the flat rate applicable to corporate assessees.

Tax liability is an important consideration guiding the choice of a legal form of business organisation. In some circumstances however this consideration is of no significance. For example large business is generally compelled to organise itself in the form of a company as this form of organisation makes it possible to raise large amounts of capital required. Similarly retail business of small size can only be economically operated as proprietorship or partnership firm. When there is freedom of choice taxation becomes an important consideration.

The relative tax burden of conducting business can be assessed by paying attention to the provisions of the Income-tax Act, 1961, Income-tax Rules, 1962 and various other notifications and circulars issued from time to time by concerned authorities.

An individual pays tax on his income on the basis of slab system. He gets the benefit of minimum taxable limit laid down by the respective Finance Acts. Income received by an individual in different capacities, i.e. as a member of a firm is not taxable in hand of partner. Because firm has paid tax on it. The owner of a proprietorship firm is treated as an individual for tax purposes.

A company is regarded as a separate legal entity. The minimum limit does not apply in its case. It is required to pay tax on every rupee of its income. Besides the usual income tax at the flat rate prescribed by the respective Finance Acts, whatever amount of tax is paid by a company is not deemed to have been paid on behalf of the shareholders. Therefore, no rebate is allowed to shareholders in this regard as is the practice in advanced countries.

(B) Partnership Firm or Limited liability Partnership

A partnership form of organization is easy to establish. The only procedure for the formation of partnership is to draw up a partnership deed and a nominal charge in terms of cost of stamps for the deed is to be incurred. This form of organization is suitable due to the following factors:

- The decision making on important business matter is quick as compared to

a company form of organization because partners meet frequently together. Therefore, decision on any important business matter cannot be delayed.

- The chance of getting involved in risky activities is very less because every important decision is made with the concurrence of all the partners.
- As compared to sole proprietorship, the problem of raising additional resources is much less. Whenever the business expands and it is necessary to raise finance, it will be easy to raise it by admitting a new partner or raising it by way of borrowings because of number of partners and their joint and several liability to pay the debts of the firm, the lenders will be more interested in lending.
- The firm can pay interest on capital and loan to partners at the maximum rate of 12% p.a. Further it can also give remuneration to its working partners subject to the limits mentioned in Section 40(b).
- This form of organisation is suitable from income-tax point of view in such cases where the amount of profit is not large and the partners of the firm do not have any other additional income except by way of remuneration and interest from the partnership firm. In such a case the profit of the firm shall be lower and the individual partners can also avail of the maximum ceiling of income exempt under the Income-tax Act.
- The share in the profit of the partnership firm is exempt from tax under Section 10(2A) of the Income-tax Act.
- The risk as to losses and liability incurred is divided amongst the partners.
- As in the case of company form of organization where the change of business requires a long procedure, there is no tedious procedure in the partnership form of organization. The business can be changed only with the consent of partners.
- The firm is taxable at a flat rate of 30% + education cess @2% + SHEC @1% for assessment year 2013-14 after allowing interest and remuneration to working partners (if provided in the partnership deed and subject to Section 40(b) of the Income-tax Act.

However this form of organization is not suitable due to the following reasons:

1. The risk taking capacity of the partners becomes limited. Every decision relating to important business matters is made with the consultation of other partners, which restricts the risk taking activities which may yield much higher profits.
2. As far as the operations of business are limited to small or medium scale, there is no problem in financing the expansion of business operation. But when business gets expanded to a large scale, then it will be suitable to adopt a company form of organization because partnership can be formed up to maximum number of 20 partners.
3. One of the main drawbacks is that one partner becomes liable for the acts of another. Therefore, a partner is liable for the wrongs of another partner if it is done within the legal limits.
4. In the new scheme of assessment of partnership firms, the share of partners is exempt from tax under Section 10(2A) but the partners remuneration and interest, subject to limit mentioned in Section 40(b), is taxable in the hands

of the partners under the head profits and gains of business or profession. Also, the firm cannot claim deduction in respect of interest payable to partners in excess of 12% per annum.

5. Where the partnership firm does not comply with the requirements of Section 184 of the Income Tax Act, although the firm shall be assessed as firm, it shall not be allowed any deduction on account of interest and remuneration to its partners.
6. A partnership firm may come to a sudden closure of business on account of death, lunacy or insolvency. In the case of a business running efficiently and profitably, such as happening will cause a great loss. Also, dissolution will attract Section 45(4) which imposes tax liability in respect of capital gain arising on transfer of capital assets from the firms to partners.

Entrepreneurs now have an alternative and innovative form of business organization i.e. Limited Liability Partnership (LLP) which combines the benefits of company and general partnership form of business organizations. LLP has separate legal entity, perpetual succession and limited liability of partners. From income tax point of view it is treated same as general partnership firm therefore its profits will be taxed in the hands of the LLP not in the hands of its partners.

(C) Sole proprietorship

The most common form of ownership found in the business world is sole proprietorship. In this form of organization, the proprietor is the only owner of the business asses and he is solely responsible for the affairs of the business.

- A sole proprietorship is easy to establish because of little interference of government regulations.
- The cost of adopting this form of organization is small because of there being no legal requirement.
- All the profits of the business go in the hands of proprietor himself.
- In case of persons carrying on business on small scale and having small income from other sources, this form of organization would be suitable because the proprietor can avail of the ceiling of exempt income as under:

For assessment year 2013-14:

(a) in case of individuals in India below 60 years of age.	2,00,000
(b) in case of individual resident in India who is of the age of 60 years or but below the age of 80 years at any time during the previous year	2,50,000
(c) in case individual who is the age of 80 years or above	5,00,000

The tax liability of the individual will be minimum as the individual is subject to income-tax at slab rate and the maximum marginal rate of income-tax in his case is 30% *plus* education cess @2% *plus* SHEC @1% for the assessment year 2013-14.

- Besides the deductions which are allowed to all assesses under Chapter VIA, a sole proprietor, being assessed as individual, is entitled to get certain deductions under the following sections:
 - (i) Section 80C relating to contributions to provident fund, life insurance premium, subscription to certain equity shares or debentures, etc.

- (ii) Section 80CCC relating to contribution to certain pension funds.
- (iii) Section 80CCD relating to contribution to notified pension scheme of the Central Government.
- (iv) Section 80D relating to medical insurance premia.
- (v) Section 80DD relating to maintenance of a dependent who is a person with disability.
- (vi) Section 80DDB relating to expenditure on medical treatment, etc.
- (vii) Section 80E relating to repayment of loan taken for higher education.
- (viii) Section 80GG relating to rent paid.
- (ix) Section 80QQB relating to royalty income, etc. of authors of certain books other than text books.
- (x) Section 80RRB relating to royalty on patents.
- (xi) Section 80U relating to persons with disability.

However, this form of organization is also not suitable due to:

- The liability of the proprietor is unlimited and it can extend even to his personal assets. When the proprietor incurs losses and business assets are not sufficient enough to meet the liabilities of business, his personal assets can be used for discharging the business liabilities.
- The proprietor does not get deduction on account of remuneration payable to him attributable to the rendering of services. It is felt that it is the capital contributed and risk taken by the proprietor for which he is rewarded in profits and that he must be given remuneration for the service rendered by him which should be allowed as deductible expenditure. But this is not so in income-tax law.
- Another main drawback of this form of organization is that it does not provide opportunities to finance the expanding business activities. In the case of a partnership firm, on the other hand, finance can be raised by the existing partners or by entering another partner.

(D) Hindu Undivided Family

A joint Hindu family pays tax on its total income at prescribed rates on the basis of slab system. The family can pay reasonable remuneration to the Karta and other family members for their services to the business and it is allowed as a deduction in computing the business income. However, interest on capital contributed by the family for the business is not deductible in computing business income. The member of the family, who has received the remuneration from the family will include it in his income under the head Salaries.

A Hindu undivided family will also get a basic exemption of ₹ 2,00,000 from assessment year 2013-14. Besides the deductions which are allowed to all assesses, it is allowed certain deductions under Sections 80C, 80D, 80DD, 80DDB and 80GG like individuals. The tax rates in case of HUF are same as applicable to individual.

The demerits of HUF, however, are similar to that of individuals.

3.8.2 LOCATIONAL ASPECTS

Tax planning is relevant from location point of view. There are certain locations which are given special tax treatment. Some of these are as under:

1. Full exemption under Section 10A for ten years in the case of a newly established industrial undertaking in free trade zones, etc. [Not allowed w.e.f. A.Y. 2012-13].
2. Full exemption under Section 10AA for initial five years, 50% for subsequent five years and further deduction of 50% for a further period of five years in the case of a newly established units in special economic zones on or after 1.4.2005.
3. Full exemption under Section 10B for 10 years in the case of a newly established 100% export-oriented undertaking. [Not allowed w.e.f. 2012-13].
4. Deduction under Section 80-IAB in respect of profits and gains by an undertaking or an enterprise engaged in the development of Special Economic Zone.
5. Deduction under Section 80-IB in the case of newly set up industrial undertaking in an industrially backward State or district.
6. Deduction under Section 80-IC in case of newly set up industrial undertaking or substantial expansion of an existing undertaking in certain special category States.
7. Deduction under Section 80-ID in respect of profits and gains from business of hotels and convention centres in specified area or a hotel at world heritage site.
8. Deduction under Section 80-IE in respect of certain undertakings in North-Eastern States.

3.8.3 NATURE OF BUSINESS

Tax planning is also relevant while deciding upon the nature of business. There are certain businesses which are granted special tax treatment. Some of them are as follows:

- Newly established industrial undertaking in free trade zones, etc. [Section 10A]. [Not allowed w.e.f. A.Y. 2012-13].
- Newly established units in special economic zones [Section 10AA].
- Newly established hundred per cent export-oriented undertakings [Section 10B]. [Not allowed w.e.f. A.Y. 2012-13].
- Tea Development Account, Coffee Development Account and Rubber Development Account [Section 33AB].
- Site restoration fund [Section 33ABA].
- Specified business eligible for deduction of Capital Expenditure [Section 35A].
- Amortisation of certain preliminary expenses [Section 35D].
- Expenditure on prospecting for certain minerals [Section 35E].
- Special reserve created by a financial corporation under Section 36(1)(viii).

- Special provision for deduction in the case of business for prospecting for mineral oil [Sections 42 and 44BB].
- Special provisions for computing profits and gains of business on presumptive basis [Section 44AD].
- Special provisions in the case of business of plying, hiring or leasing goods carriages [Section 44AE].
- Special provisions in the case of shipping business in the case of non-residents [Section 44B].
- Special provisions in the case of business of operation of aircraft [Section 44BBA].
- Special provisions in the case of certain turnkey power projects [Section 44BBB].
- Special provisions in the case of royalty income of foreign companies [Section 44D].
- Special provisions in case of royalty income of non-residents [Section 44DA].
- Profit and gains of industrial undertakings or enterprises engaged in infrastructure development, etc. [Section 80-IA].
- Profits and gains of an undertaking or an enterprise engaged in development of Special Economic Zone. [Section 80-IAB].
- Profits and gains from certain industrial undertaking other than infrastructure development undertaking [Section 80-IB].
- Special provisions in respect of certain undertakings or enterprises in certain special category States [Section 80-IC].
- Deduction in respect of profits and gains from business of hotels and convention centres in specified area or a hotel at world heritage site. [Section 80-ID].
- Special provisions in respect of certain undertakings in North-Eastern States. [Section 80-IE].
- Profits and gains from the business of collecting and processing of bio-degradable waste [Section 80JJA].
- Employment of new workmen [Section 80JJAA].
- Special tax rate under Sections 115A, 115AB, 115AC, 115AD, 115B, 115BB, 115BA and 115D.

3.8.4 MEASURES OF TAX PLANNING RELATING TO CORPORATE RESTRUCTURING

The following suggestions could be useful for tax planning in respect of amalgamation merger, demerger, etc.

1. Since the unabsorbed losses and unabsorbed depreciation cannot be allowed to be carried forward and set off in the hands of the amalgamated company, except in the cases prescribed under Section 72A of the Act, it is

proposed:

- (a) that the scheme of the amalgamation can be put off till such time the full benefit of set off is availed of by the amalgamating company; and
 - (b) that the loss carrying company should absorb or take over the business of the profit-making company. In other words, the profit making company should merge itself with the loss incurring company. This would help in carrying to carry forward the benefits of all unabsorbed losses and depreciation to be set off against the profits derived from the business of the profit-making company.
2. To save from disallowance of the debts of the amalgamating company which subsequently become bad in the hands of the amalgamated company, the amalgamated company should plan to make suitable provision for the expected losses on account of bad debts at the time of fixing the consideration while taking over the business of the amalgamated company.

However, in view of the Court judgment of *CIT v. T. Veerabhadra Rao* (1985) 22 Taxmann 45, the bad debts are not allowed to an assessee by way of personal relief but to a business. So, it is possible for the amalgamated company to claim bad debts even in respect of debts taken over from the amalgamating company.

3. A company whose shares are not quoted on a recognised stock exchange may avail the benefit of amalgamation by amalgamating itself with another company whose shares are quoted on a recognised stock exchange. This would help its shareholders to take the advantage of the quoted price of their shares in the stock exchange while determining their liability for wealth-tax purposes.
4. A company holding investments in immovable properties may avail the benefit of non-applicability of the provisions of the Urban Land Ceiling Act by amalgamating itself with an industrial company.
5. A loss incurring company and a profit-making company may merge in order to reduce the overall incidence of liabilities to tax under the Income Tax Act, 1961.
6. In case the conditions provided under Sections 2(1B) and 72A of the Act are not satisfied, it may be suggested that the profit making company should merge itself with the loss making company, so that the loss making company does not lose its existence and also enjoys all other benefits.
7. Under Section 2(1B) of the Act, it is provided that for availing the benefits of amalgamation, at least 75% of the shareholders of the amalgamating company should become shareholders of the amalgamated company. In case more than 25% of the shareholders are not willing to become shareholders of the amalgamated company, it is proposed that the amalgamating company may persuade the other shareholders who may be willing, to purchase the shares in the amalgamated company to acquire the shares of the remaining shareholders so that the percentage of dissenting

shareholders does not exceed 25%. Alternatively, the amalgamated company prior to, amalgamation, may purchase shares from such dissenting shareholders so as to make such dissenting shareholders to go below the specified percentage of 25%.

There is a recent trend of going in for reverse merger. It means that the profit making company merges into the sick company thereby becoming eligible to carry forward of losses etc. without the aid of Section 72A of the Act. The profit making or healthy company extincts and loses its name and the surviving sick company retains its name. It is actually device to bypassing merger under Section 72A of the Act and is being increasingly popular now a days.

Invariably soon after the merger or after a year or so, the name of the company is changed to accord with that of the profit making amalgamating company in this way two birds are killed with one stone because : (1) Losses are carried forward, which would otherwise have not been possible; (2) Goodwill, which consists, in the name of the profit making amalgamating company, is also retained. The same route was followed, among others, by Kirloskar Pneumatics Ltd. where the company merged with Kirloskar Tractors Ltd., a sick unit and initially lost its name but after one year it changed its name as was prior to merger. However, it remains to be seen whether the Parliament/Judiciary views this kind of strategy as an exercise resulting in tax-avoidance or not? But, right now, this is not required in view of changes done in Section 2(1B) and 72A of the Act.

3.8.5 TAX PLANNING RELATING TO FINANCIAL MANAGEMENT DECISIONS

When a company raises long term loans from financial institutions or by way of public issue of debentures or inviting deposits from the public, it should plan that the expenses incurred on such issues of debentures or expenses towards stamp duty, registration fees, and lawyer's fees should be incurred only after the date of the 'setting-up' of the business. The interest paid before the commencement of production but after setting up of the business on loans taken by the company for the acquisition of its plant and machinery and other assets, forms part of the actual cost of the asset and it should be capitalized in actual cost of asset. Thus, the company would be allowed to capitalise the expenditure and claim a higher depreciation and investment allowance.

The company should also plan the optimum use of the share capital and the borrowed funds. Note that the borrowings should be utilised as far as possible for the acquisition and installation of assets like, buildings, plant and machinery so that interest can be capitalised for the period after setting up of the acquired assets like buildings, plant and machinery but before the commencement of production. The interest and higher amount of depreciation (due to capitalisation of expense) may be claimed as revenue expenditure pertaining to the business of the company.

The company should also plan to purchase the depreciable assets on credit terms and an agreed amount of interest can be paid on such credit purchases or the company may purchase these company assets on the basis of the hire purchase agreement enabling the company to claim the amount of interest paid as revenue business expenditure. The company would also be entitled to claim either the depreciation for use of the asset or may treat the hire charges as the rent for the asset in the normal course of business and claim deduction on revenue account.

The following table will help the finance manager framing suitable plans relating to capital structure:

	<i>Capital</i>	<i>Borrowings</i>	
(a)	Dividend/Interest	Not deductible	Fully deductible
(b)	Cost of raising finance	1/5th allowed under Section 35D	Fully deductible in first year.

Taking the same sources of finance, the comparison between pre-commencement period and post-commencement period is as follows :

- (a) (i) Dividend is not deductible either for pre-commencement period or in the post-commencement period in India.
- (ii) Interest is capitalised for pre-commencement period, i.e. added to the cost of project' (cost of fixed assets) and its depreciation is calculated on capitalised value of assets. In post-commencement period, interest is fully deductible.
- (b) (i) Cost of raising finance in case of capital is not deductible as revenue expenditure but amortised under Section 35D of the Act. If such expenditure is incurred after the commencement of the business. Section 35D is applicable, provided the expenditure is undertaken for expansion purposes in case of industrial undertaking.
- (ii) Cost of borrowing funds in case of pre-commencement period is capitalised and in case of post-commencement period, it is deductible fully in the year.

The above consideration will go a long way in suggesting the managements of corporate entities to adopt a suitable capital structure and selecting the appropriate financing sources by providing an optimum capital mix for the organization

3.8.6 TAX PLANNING RELATING NON-RESIDENTS

Suggested tax planning measures for Non-Resident are:

1. As a Non-resident is not required to pay tax on his income earned and received outside India, an Indian citizen having an assignment abroad could plan his visits to India in such a way so that he could remain to be a Non-Resident for the purpose of the Income Tax Act. This is generally of interest to persons employed in foreign countries.
2. All those dealing with Non-Residents must keep in view the provisions of Sections 162 and 163. They should retain sufficient amounts with them to be paid on behalf of the Non-Resident towards his tax liability, so that they are not obliged to pay such taxes on their own account. They should also keep in view the obligations cast by Section 200, of paying the taxes deducted within the time prescribed so as to avoid applicability of the prosecution provisions under Section 276B.
3. A Non-resident must be very clear as regards his tax liability through agent.

He must be aware that the agent will deduct some amount out of the amount payable to the Non-Resident.

4. Persons employed by or on behalf of a Non-Resident, those who have a business connection with Non-Resident and statutory agents are all considered as authorised agents of a Non-Resident. Even a Non-Resident could be treated as the agent of another Non-Resident.
5. It should be remembered that if the agent is unable to recover from the Non-Resident the amount of tax paid on his behalf, he cannot claim it as a bad debt or as business loss in view of Supreme Court decision in *CIT v. Abdullabhai Abdhulkadar* (1961 41 ITR 545).
6. Another very important point is the close financial association between a resident and a Non-Resident. This can also amount to a business connection. In a case where all Indian Banks and a foreign bank were controlled by the same persons and the main function of the foreign bank was to finance the Indian Bank, it was held that a business connection existed in India between the two banks, *Bank of Chettinad Ltd. v. CIT Madras* (PC) (1940) 8 ITR 522.
7. When an individual, being a citizen of India leaves India for purposes of employment, the new explanation under Section 6(1)(c) mitigates the rigor of the provisions about treating a person as resident and ordinarily resident. Under clause (c), an individual is said to be resident in India in any previous year if having been in India for at least 365 days during the four preceding years, he is in India for 60 days in that year. Clause (a) of the new explanation provides that where an individual citizen leaves India in any previous year as a member of the crew of an Indian ship as defined in clause (18) of Section 3 of the Merchant Shipping Act, 1958 (44 of 1958); or for purpose of employment outside India, the period of 60 days will be substituted by 182 days. Likewise, clause (b) provides that where an Indian citizen or a person of Indian origin within the meaning of Explanation to Clause (e) of Section 115C who is outside India comes on a visit to India in, the previous year, the period of 60 days referred to in sub-clause (c) will be substituted by 182 days. Thus, they will be Non-Resident in India for that year and as a result salary income earned abroad will not be taxed in India. They may visit India during vacation for 181 days or less, or else if he desires to stay in India for a period longer than 181 days the visit should be so planned over two previous years that his total stay in any one previous year should remain 181 days or less.

Explanation to Section 6(1)(c) had been substituted by Direct Tax Laws (Second Amendment) Act, 1989 and subsequently amended by the Finance Act, 1990 with effect from 1.4.1990 i.e. for and from the assessment year 1990-91. Under the substituted Explanation, it is provided that in the case of an Individual:

- (a) being a citizen of India, who leaves India in any previous year as a member of the crew of an Indian ship as defined under Section 3(18) of the Merchant Shipping Act, 1958 (44 of 1958, or for the purposes of employment outside India, the provisions of Section 6(1)(c) shall apply in relation to that year as

if for the words 'sixty days', the words 'one hundred and eighty two days' had been substituted.

- (b) being a citizen of India, or a person of Indian origin within the meaning of Explanation to Section 115C(e), who being outside India, comes on a visit to India in any previous year, the provisions of Section 6(1)(c) shall apply in relation to that year as if for the words 'sixty days' occurring therein, the words 'one hundred and eighty two days' had been substituted.

3.8.7 TAX PLANNING FOR INDIAN COLLABORATORS

While entering into an agreement for foreign collaboration, the Indian collaborator should take into consideration such aspects as will enable him to plan his tax affairs in a manner that ensures maximum after-tax profits and return on investment. In this context, the Indian collaborator may be advised to adopt the following steps for tax planning:

- (i) **Capitalisation of installation expenses** : As far as purchase of capital goods from the foreign collaborator is concerned, it is needless to say that this is a capital expenditure on which depreciation is admissible. But care should be taken to see that the cost of installation, including the supervision expenses charged by the collaborator, is also capitalised and depreciation claimed thereon, The Indian company should also be vigilant that the other expenses relating to the collaboration agreement must be incurred after the date of the setting up of the business, because only then it would be entitled to be capitalised as other expenses.
- (ii) **Treating purchase of spares as revenue expenditure** : For the purchase of spares for the plant, the Indian collaborator should plan to receive the spares subsequent to the year of commissioning of the plant and preferably execute a separate contract in this behalf. It will enable the Indian company to treat the whole of the amount of spares as revenue expenditure. In this context, the judgement of the Madras High Court in *CIT v. Rama Sugar Mills Ltd.* (1052) 21 ITR 191 (Mad.) is worth-noting. A sugar manufacturing company had three boilers at its factories. Two of these were constantly in use and the third one was kept as "spare" ready to be used when one of the other two boilers had to be cleaned up at intervals. The productive capacity of one of the boilers deteriorated and the company was required to purchase the other at a cost of ₹ 85,000. The Madras High Court held that this expenditure was deductible on revenue account, on the ground that "the boiler which was substituted was exactly similar to the old one and by this expenditure, the assessee company did not bring any additional advantage to the trade or business, which they were carrying on and there is no improvement. It cannot be suggested that by using a new boiler for an old one, the production capacity of the sugar manufacturing unit was in any manner increased".
- (iii) **Treating plans and drawings, etc. as "Plant for availing of full value as depreciation"**: In view of the Supreme Court's decision in the case *CIT v. Alps Theatre*, (1067) 65 ITR T77 (S.C.) "Plant" includes ships, vehicles, books, scientific apparatus, and surgical equipments used for the purpose of business or profession.

However, know how acquired on or after 1.4.1998, owned wholly or partly by the assessee and used by such assessee for the purpose of his business or profession, will form a separate block of asset alongwith other intangible asset and will be eligible for depreciation under section 32(1) @ 25% on written law value.

3.8.8 TAX PLANNING FOR EMPLOYEES

The employees should keep the following aspects in view while planning their salary package:

- (i) The employee should opt for division of salary into basic pay and allowances and should not opt for the consolidated salary. This will minimise his tax incidence considerably as some of the allowances are exempt from tax upto a certain extent for e.g. conveyance allowance is exempt upto ₹800 p.m.
- (ii) Under the terms of employment, dearness allowance should form part of the retirement benefits. This will not only increase the employees retirement benefits but also reduce his tax incidence in respect of HRA, gratuity, commuted pension, employer's contribution to RPF, etc.
- (iii) Any commission payable as per the terms of employment should be based on turnover so as to form part of salary. This will also reduce the tax incidence in respect of HRA, commuted pension, interest credited to RPF, etc.
- (iv) If the employee is allowed the use of more than one car for his private purposes, the horse power of any such car should not exceed 1.6 litre cubic capacity as otherwise he shall be deemed to have been provided with one car of 1.6 cubic litre capacity which would lead to higher valuation of such persuite.
- (v) The employer's contribution to RPF should be 12% of salary as it is exempt upto this limit.
- (vi) The employee should opt for re-imbusement of expenses on medical treatment (on free medical facility) in place of medical allowance because such allowance is taxable whereas the reimbursement is not taxable upto the extent of ₹ 15,000. The same thing holds good for entertainment allowance.
- (vii) Perquisites should be preferred to taxable allowances. This shall help not only in lower valuation of a perquisite like rent free house but the employee will also be free from falling into the category of specified employees.
- (viii) It may be noted that if furniture is provided without rent free accommodation, it will not be taxable in the hands of non-specified employees.
- (ix) An employee who resigns before completing five years of continuous service in an organisation, should ensure that the new organisation he joins maintains RPF so that the accumulated balance of the provident fund could be transferred to the new organisation to claim exemption thereon.

- (x) On retirement, the employee should opt for commuted pension to the maximum permissible limit as it is exempt from tax within certain limits.
- (xi) Leave encashment should preferably be done on termination of employment by superannuation or otherwise as it will then be exempt from tax within certain limits.

In addition to the above, the employees should also plan for taking full advantage of the relevant provisions under Section 80 of the Income Tax Act.

3.8.9 TAX PLANNING UNDER WEALTH TAX ACT

As measures of tax planning, companies can take the following precautions:

- (a) As far as possible, companies should avoid to invest in taxable assets like, jewellery, motor cars, other unproductive assets etc.
- (b) Alternatively, in unavoidable cases, the investment in the said assets could be made out of loan or a debt may be incurred in relation thereto, by way of furnishing a security for a loan. For example, companies generally finance the purchase of assets like, motor cars/trucks/vehicles etc., through bank loans/overdrafts/mortgage.
- (c) Likewise, purchase of a house property likely to be used by the Directors/ Manager/Secretary as their residential accommodation or by any other employee who has a substantial interest in the company (holding at least 10% equity shares of the company) could be funded out of loan/raising of debts thereon.

The strategy will help the company to dilute the incidence of tax on its wealth.

3.8.10 CHARITABLE INSTITUTIONS

Associations having charitable object viz., promotion of commerce, art, science, religion, charity or any other useful object by nature, can be registered as companies under Section 25 of the Companies Act, 1956, and avail the benefits of a company form of organisation from the point of view of the Companies Act, as well as the various tax concessions available to widely-held companies under the Income tax Act and also claim exemption from, Wealth tax and total exemption from Income tax under Section 11 of the Income Tax Act subject to the conditions specified in Section 13 thereof.

3.9 PLANNING IN THE CONTEXT OF COURT RULINGS AND LEGISLATIVE AMENDMENTS

It is a common feature of modern legislative system to lay down in the Acts, the principles and the policy of the legislature leaving out details to be filled-in or worked-out by rules or regulations made either by the Government or by some other authority as may be empowered in the legislations. This kind of subordinate or administrative legislation is justified and even necessitated by the fact that the legislature has neither the time nor the material to consider and act with reference to various details. Not only that they may not be even acquainted fully with the facts and

circumstances relating to the subject matter. Section 295(1) of the Income-tax Act and Section 46(1) of the Wealth Tax Act respectively vest in the Central Board of Direct Taxes the power to give retrospective effect to any of the rules in such a way as not to prejudicially affect the interest of the tax payers.

The various matters in respect of which the rules may be framed are specified in the relevant sections. Section 119 read together with Section 295 empowers Central Board for Direct Taxes to frame rules, issue circulars, notifications, administrative instructions to the sub-ordinate authority for smooth functioning of the Income Tax Act, 1961. Section 119 read together with Section 295 gives general powers to Central Board for Direct Taxes to frame the rules and notifications. However, relevant sections empower Central Board for Direct Taxes to frames rules and issue relevant notifications. For example, Section 44AA provides that certain persons carrying on profession or business such as legal, medical, architectural or interior decoration or the profession of accountancy or technical consultancy or any other profession as is notified by the Board. Therefore, on careful perusal of Section 44AA, it may be seen that this Section empowers Central Board for Direct Taxes to issue notification to the effect that other professions shall be covered by the provision of Section 44AA for maintenance of books of account.

3.10 STATUTORY FORCE OF THE NOTIFICATIONS

Section 296 of the Income Tax Act, 1961 provides that the Central Government shall cause every rule made under this Act or for that matter any notification issued, to place before both the Houses of Parliament either before issuing them or in case same is issued when Parliament is not in session immediately thereafter when the Houses are in session. Rules and notifications are made by the appropriate authority in exercise of the power conferred on it under the provisions of the Act. For the A.Y. 2008-09, notification includes every notification issued before the 1-6-07 under Section 10(23C)(iv). Therefore, they have statutory force and can be equated to the law made by the legislature itself. Thus, they are a part and parcel of the enactment. The rules cannot, however, take away what is expressly conferred by the Act. In other words, they cannot whittle down the effect of the law. The rules are only made in consonance with provisions of the Act. They must be interpreted in the light of the section under which they are made. If there is any irreconcilable conflict between a rule and a provision in the Act, the provision in the Act will prevail.

Notifications when validly made in exercise of the authority provided for in the law, are equally binding on all concerned and may be enforced. (As for press notes, although they have no statutory force as such, they are binding on the officers). Section 119(1) of the Income-tax Act provides that all officers and other persons employed in the execution of the said Act shall observe and follow the orders, instructions and directions of the Board, provided that such orders, instructions or directions shall be issued as not to interfere with the discretion of the Appellate

Assistant Commissioner in the exercise of his appellate functions. It is judicially settled that the circulars issued by the Board would be binding under Section 119 on all the officers and persons employed in the execution of the Act [*Navnital Javeri v. Sen* (1965) 56 ITR 198 (SC)]. If an Income Tax Officer contravenes any circular issued by

the CBDT in any respect, he can be called-upon by the appropriate authority including the Commissioner/Commissioner (Appeals), and the Appellate Tribunal to give effect to it. Though the Circular is not the same footing as a rule, it can be taken judicial note of. However, it may be noted that an opinion expressed by the Board in individual communications to the assessee (for example, as to when the new industrial undertaking established by the assessee began to manufacture or produce articles within the meaning of Section 80(I) cannot be considered as directions binding on the income tax authorities under Section 119. The Board is not competent to give directions where the exercise of any quasi judicial discretion by the subordinate authorities in individual cases is involved. [*J.K. Synthetics Ltd. v. CBDT* (1972) 83 ITR 335 (SC)]. It has been clarified by the Supreme Court in *Kerala Financial Corporation v. CIT* 210 ITR 129 that Section 119 does not empower the CBDT to issue order, instruction or direction overriding the provisions of the Act. That would be destructive of all known principles of law as the same would really amount to giving power to a delegated authority to even amend the provisions of law enacted by the Parliament. Under Section 119 CBDT also cannot issue order for a specific case.

Normally, exemptions should be specifically provided by the Statute giving exemptions. Where schedules and notifications are issued as empowered by the statute, the exemptions given by the notification would be legally valid as if were given by the statute itself. In the case of *Collector of Central Excise v. Parle Exports (P) Ltd.* (1990, 183 ITR 624), the Supreme Court had held that when a notification is issued in accordance with powers conferred by the statute, it has statutory force and validity and therefore, it is as if the exemptions under the notification were contained in the Act itself.

The various judicial rulings point out the following::

- (1) *The instructions of the Board are binding on the Department but not on the assessee.*
- (2) *The instructions have to be followed by the Departmental Officers. Instruction adverse to an assessee's interest can be challenged by him.*
- (3) *The instructions withdrawn subsequently should be given effect to by the Assessing Officer for the assessment year for which they were in force even though they are withdrawn at the time he makes the assessment.*
- (4) *In the exercise of its power, the Board cannot impose a burden or put the assessee in a worse position.*

In view of this position, the tax planner, while planning his affairs or that of his clients must take into account not only the relevant legal provisions which affect him but also all relevant rules, notifications, circulars etc. As for circulars, since they are in the nature of administrative or executive instructions, the possibility that they might be withdrawn by the Board at any time, should also be taken into account. They may be challenged in the courts although, otherwise, they are binding at the administrative level. In cases where the circulars are based on an erroneous or untenable footing, they are liable to be quashed by the courts.

3.11 ORGANISATION OF TAX PLANNING CELLS

Some companies can afford to have separate tax planning departments while

others cannot. The need for having tax planning department does not depend upon the amount of tax liability of the company. In fact, in certain cases, companies having effective tax planning cells can plan their transactions with a view to attract the least incidence of tax organisation of such a cell can be justified on the following grounds :

- (a) **Complexity and volume of work:** Where the volume of tax work to be handled is large and highly complex, then it is required to appoint a special tax expert along with the required staff.
- (b) **Separate Documentation:** Documentation is an indispensable ingredient of tax management. An assessee has to keep reliable, complete and updated documentation for all the relevant tax files so that the documentary evidence can be made available at a short notice whenever it is required. In absence thereof, an assessee may lose a case for want of proper documentary evidence. Not only that the company has to maintain proper account books, records, vouchers, bills, correspondence and agreements, etc. as a part of tax management. In the case of new industrial undertaking it is better to keep separate accounts for the same.
- (c) **Data Collection :** The staff concerned with taxation has to collect and keep on collecting data relating to latest circulars, case laws, rules and provisions, and other government notifications to keep abreast of the current developments. This could also guide them in any particular area, when such guidance is needed. The composition of organisation of such data bank may vary from one organisation to another. However, keeping in view the general areas of operation of the company, it may, be advisable to arrange the data in the order of subject sequence. This would enable easy availability of information at the relevant time.
- (d) **Integration :** Tax planner should be consulted by all the departments of the company to know the impact of taxation on their decisions. It would be necessary to integrate and properly link all the departments of the company with the tax planning department. Any project or blue print may have a tax angle. This has to be identified early enough to facilitate better tax compliance and availing of the several incentives. The department has to deal with all taxes (both State, Central and Local Self Governments).
- (e) **Constant Monitoring :** In order to obtain the intended tax benefits, persons connected with tax management should ensure compliance of all the pre-requisites, like procedures, rules etc. Besides, there should be constant monitoring, so that all the tax obligations are discharged and penal consequences avoided.
- (f) **Developing Tax effective Alternatives :** A managerial decision could be assumed to have been well taken only if all the pros and cons are considered. A tax planner could guide important decisions, by considering varieties of alternatives and choices.
- (g) **Take advantage of variance allowances and deductions :** A tax manager has to keep track of the provisions relating to various allowances, deductions, exemptions, and rebates so as to initiate tax planning measures. The details of various tax incentives have been duly dealt with in the relevant studies in this book.

3.12 OVERALL TAX PLANNING MEASURES

Apart from location and nature of business, form of organisation is another important area where tax planning with reference to setting up a new business could be exercised. In Study III, it has been concluded that in most cases, company form of organisation is to be preferred from long-term point of view. There are, however, certain other dimensions in this context. One such dimension is the preference for a widely held company as against a closely held company so much that we would suggest conversion of an existing closely held company into a widely held company because a widely held company would be able to enjoy the following tax benefits over a closely held company.

- (a) Widely-held companies do not find limitations and restrictions in the matter of set off and carry forward of losses whereas closely-held companies have certain limitations or restrictions in this respect under the provisions of Section 79 of the Act. In the case of companies in which the public are not substantially interested, losses will not be carried forward and set off unless: the shares of the company carrying not, less than 51 per cent of the voting power were beneficially held by the same person(s) both on the last day of the previous year in which loss occurred and on the last day of the previous year in which brought forward loss is sought to be set off.

However, if a change in voting power as aforesaid takes place consequent upon the death of a shareholder or on account of transfer of shares by way of gift to any relative of the shareholder making such gift, then the aforesaid disability does not get attracted. This disability is also not attracted where change in the shareholding of an Indian company which is a subsidiary of a foreign company, take place as a result of amalgamation or demerger of a foreign company subject to the condition that fifty one percent shareholders of the amalgamating or demerged foreign company continue to be the shareholders of the amalgamated or the resulting foreign company.

The provisions of Section 79 of the Act are applicable in the case of carry forward and set-off of losses only. As carry forward of unabsorbed depreciation allowance, investment allowance, development rebates and development allowance stands on an altogether different footing; their carry forward and set off is not governed by Section 79 of the Act in view of the decision of Madras High Court in *CIT v. Concord Industries Ltd.* (1979) 119 ITR 458 (Madras).

The Madras High Court's decision was later followed by the Kerala High Court in *Commissioner of Income Tax v. Kalpaka Enterprises (P) Ltd.* 986, 157 ITR 658 holding that Section 79 of the Income Tax Act, 1961 overrides the other provisions in Chapter VI and not the other provisions in the Act itself as is clear from the opening words 'Notwithstanding anything contained in this Chapter'. The connotation of the expression 'loss' occurring in Section 79 has thus to be understood in the context of the provisions contained in Chapter VI itself. The 'loss' mentioned in Section 79 is relatable to the 'loss' specifically provided for in the other provisions of the said Chapter. It is in respect of losses which could be carried forward and set off under the said Chapter that Section 79 operates to

limit that set off only to the previous year in question without extending it to any prior years. The Act does not treat or describe 'unabsorbed depreciation' or 'unabsorbed development rebate' as losses and these items cannot be treated as losses for purposes of Section 79. Hence, the bar imposed under Section 79 does not apply to 'unabsorbed depreciation' or 'unabsorbed development rebate'.

In this case, while finalising the assessment for the year 1969-70, the Income-tax Officer, after adjusting the losses brought forward from the preceding three years, determined the total income, as nil and also recorded *inter alia*, that unabsorbed depreciation for the prior years 1964-65 should be carried forward. The order of the income-tax Officer was set aside by the Commissioner in view of the fact that the officer had allowed set-off of the earlier year's losses against the profits of the year without considering the question of the applicability of Section 79 of the Act. The Tribunal, however, held that Section 79 of the Act did not apply to the unabsorbed depreciation and development rebate. On a reference to the High Court, the Court held that the Tribunal was right in holding that the provisions of Section 79 of the Act prohibiting the carry forward of losses in certain Companies would not apply to unabsorbed depreciation and development rebate.

- (b) The provisions of 'deemed dividend' in respect of advances or loans to shareholders, or any payment on behalf of shareholders or any payment for the individual benefit of a shareholder are applicable to closely held companies under Section 2(22)(e) of the Act.
- (c) The conversion would not be treated as transfer of ownership of the business and hence, there shall be no liability for capital-gains tax or Income tax in the hands of the closely-held company or the new widely-held company, due to conversion.

3.13 SOME GENERAL CONSIDERATIONS REGARDING NEW BUSINESS

1. *Separate Accounts*: It is advisable, though not a statutory obligation, to keep the accounts of the new business separate. This obviates the necessity of making any estimates, complicating the state of affairs of the new business. In this connection, reference may be made to *CIT v. Dunlop Rubber Co. (I) Ltd.*, 1977 (107 ITR 182).

In this case, the existing company established a new factory and no separate accounts were maintained by the new unit. But, as a matter of fact, this was not essential for claiming the benefit. In this case the assessee claimed the benefit on the proportion of turnover between the new unit and old unit. Was the method adopted correct? The duty of Revenue Department was to determine the exemption allowed by law.

It was held : "it was the duty of the I.T.O. under Sections 143 to 145 of the Act, to determine the total income of the assessee and determine the tax payable, even if the income could not be derived from the books of the assessee. So, Income-tax Officer cannot deny the relief. Difficulty in computing the relief cannot be a ground for rejecting the claim. A rule of apportionment consistent with commercial accounting must be evolved in computing the income. If the assessee already followed certain

system, which is in vogue in general, from a commercial accounting angle, and if the Income-tax Officer disputes such system he should correct it and cannot reject it as whole-sum. In this case it was held that the Income-tax Officer could not refuse the claim for exemption.

Supreme Court in *Textile Machinery Corporation Ltd. v. Commissioner of Income-tax* (1977 108 ITR 195) inter-alia, held that the fact that there was common management or the fact that separate accounts had not been maintained, would not lead to the conclusion that they were not separate undertakings. Even if separate account is not maintained, the investment in each of the units can be reasonably determined with the material which the assessee may make available to the department. The test is whether it is a new and identifiable undertaking separate and distinct from the existing business. It is sufficient if the new undertaking is an integrated unit by itself wherein articles are produced and a minimum of 10 persons are employed. In *Mahindra Sintered Products Ltd.* (1989, 177, ITR 111), the Bombay High Court held that it was not necessary that separate accounts had to be maintained but separate accounts kept in the ledger are sufficient to claim deduction under Section 80J.

Following the ratio laid down by the Bombay High Court in the case of *Mahindra Sintered Products Ltd.* (supra) the Patna High Court held that in order to claim special deduction under Section 80J, the following facts have to be established by the assessee namely:

- (i) investment of substantial fresh capital in the new industrial undertaking set up,
- (ii) employment of requisite labour therein,
- (iii) manufacture or production of articles on the said undertaking,
- (iv) earning of profits clearly attributable to the said undertaking, and
- (v) above all, a separate and distinct identity of the industrial unit set up.

The fact that there was common management or the fact that the separate accounts had not been maintained or that there was a common source of power would not mean that it was not a new undertaking. The assessee was held entitled for relief under Section 80J.

Following its judgement in the case of *Mahindra Sintered Products Ltd.* (supra) the Bombay High Court held in *Commissioner of Income-tax v. Mazaggon Dock Ltd.* (1991, 191 ITR 461) that the maintenance of separate accounts is not a condition precedent for claiming special deduction under Section 80J. Since the frigate project was a new one and the capital outlay was many times more than the assessee's capital, the assessee was entitled to deduction under Section 80J.

Though Section 80J is omitted with effect from 1.4.89, the ratio is applicable on other deduction available.

2. Avoid interconnection of service or departmental centralisation or pooling of resources of the new business and any other activity of the assessee. In this connection, a reference may be made to *T. Satish U. Pai v. CIT* 119 ITR 877 (Kar).

3. Avoid, transfer of goods between the new business and the assessee's other activities and encourage only cash flows out of sale proceeds towards investment or capital purpose.

4. It is better for the new business to have separate floor area, separate licenses and agreements, if it is not related to the assessee at all. Even separate profit computation should be encouraged. But the total income should be computed as per the scheme of the Act. [*CIT v. Kashmir Fruit and Chemical Industries*, 1975 98 ITR 311 (J & K)].

5. In case of capital intensive industries having long gestation periods; generally profit earning would be delayed. This is true even in the case of complicated and time-consuming manufacturing processes. In such circumstances, it is quite likely that only 'deficiency' would be absorbed.

6. Each industrial unit (for example, weaving and spinning units in case of textile business) of an industrial organisation has to be considered for computing the tax holiday benefit.

7. Any capital or revenue expenditure incurred towards scientific research under Section 35, will be treated as mentioned therein.

3.14 SETTING UP AND COMMENCEMENT OF BUSINESS VIS-A-VIS TAX PLANNING

Setting up a business within the scope of the Income Tax Act is a particular point to be considered for the purpose of tax planning strategy. It is different from the commencement of business. The company may be incurring certain expenditure of revenue nature during the intervening period after setting up and before the commencement of business (production). It is provided in the tax laws that the general expenses prior to the date of setting up are inadmissible but those incurred from the date of setting up and before the commencement of the business may be allowed as deduction for tax purposes provided they are of revenue nature and are incurred wholly and exclusively for the purpose of business.

From the decisions of the Bombay High Court in *Western India Vegetable Products Ltd. v. CIT* [(1954) 26 ITR 151 (Bom)] and the Supreme Court in *CIT v. Ramaraju Surgical Cotton Mills Ltd.* [(1967) 63 ITR 478 (SC)] and *Travancore Cochin Chemical Pvt. Ltd. v. CIT* [(1967) 65 ITR 651 (SC)], it has been well settled that a business is set up as soon as it is ready to commence production and it is not necessary that the actual production should be so commenced. It is also observed that the business commences with the start of first activity in point of time and which must necessarily precede other activity.

In the case of *CIT v. Saurashtra Cement and Chemical Industries Ltd.* [(1973) 91 ITR 170 (Guj.)], the decision of the Gujarat High Court is worth noting. In this case the company was established for manufacturing cement. The court observed that:

“the business is set up as soon as acquiring of lime stone is commenced even if at that time, the plant and machinery may not have been installed so that actual manufacturing operations may commence. They have expressed the view that the business commences with the start of activity which is first in point of time and which

must necessarily precede other activities. The court observed that the business comprises several activities. Starting of one of those activities may in some circumstances fulfil the principal condition of setting up of a business. All the activities of the business need not be started simultaneously. But when an activity, which is the first in order of sequence preceding other activities is started, then it can be said that the company has been set up.”

In the case of *Commissioner of Income-tax v. Saurashtra Cement and Chemical Industries Ltd.* (1973, 91 ITR 170) the Gujarat High court had, *inter alia*, held that ‘Business’ connoted a continuous course of activities. All the activities which go to make up the business need not be started simultaneously in order that the business may commence. The business would commence when the activity which is first in point of time and which must necessarily precede all other activities is started.

Reliance on the above case was placed by the Allahabad High Court in the case of *Mod Industries Ltd. v. Commissioner of Income Tax* (1977, 110 ITR 855) while deciding the question of allowance of business expenditure, it was held in this case that the foreign tour expenses of the chairman for setting up of two new factories were not - allowable as business expenditure under Section 37 and were of a capital nature.

The ruling of the Gujarat High Court was applied by it in the case of *Hotel Alankar v. Commissioner of Income Tax* (1982, 133 ITR 866) holding that when a business is established and is ready to commence business, it can be said of that business that it has been set up. The words ‘ready to commence’ would not necessarily mean that all the integrated activities are fully carried out and/or Wholly completed. This requirement is also complied with in a given case where an assessee had undertaken the first of the kind of integrated activities of which the business in overall comprised of, the question whether a business has been set-up or not is always a question of fact which has to be decided on the facts and in the circumstances of the case subject to the broad guidelines provided by different decisions in that behalf.

With regard to setting up of business or commencement of business, there is another decision of the Gujarat High Court in the case of *Sarabhai Management Corporation Ltd. v. Commissioner of Income Tax* (1976), 102 ITR 25 where it has held that, it is only after the business is setup that the previous year of that business commences and any expenses incurred prior to the setting up of a business would be of capital nature and not a permissible deduction. There may, however, be an interval between the setting up of the business and the commencement of the business, all expenses incurred during that interval would be a permissible deduction. Applying this decision, the Punjab and Haryana High Court in the case of *Commissioner of Income-tax v. O.P. Khanna and Sons* (1983, 140 ITR 558) (the assessee carried on business of printing press, purchased a new building in November 1970, installed electrical fittings and shifted to the building in Sept. 1971) held that during transitory period the building had been ‘used’ by the assessee and the depreciation allowance had to be made in respect of it while computing its business income.

The Gujarat High Courts’ decision in the case of Sahabhai Management Corporation Ltd. (supra) had been affirmed by the Supreme Court in *Commissioner*

of Income Tax v. Sarabhai Management Corporation Ltd. (1991, 192 ITR 151) holding that even if the acquisition of the property for being let out could be said to be only the preparatory stage, the subsequent activities constituted activities in the course of the carrying on the assessee's business. It was not correct to treat the assessee as having commenced business only when the licensee or leasee occupied the premises or started paying rent. The High Court was held to be right in interfering with the finding of the Tribunal which was based on a mis-direction in law.

The Andhra Pradesh High Court laid down the following principles to determine whether a business has commenced or not in *Commissioner Income Tax v. Sponge Iron India Ltd.* (1993, 201 ITR 770):

Whether a business has commenced or not is a question of fact.

- (i) *There is a distinction between the setting up of business and the commencement of business.*
- (ii) *Where the business consists of a continuous course of activities, for commencement of business all the activities which go to make up the business need not be started simultaneously. As soon as an activity which has the essential activity in the course of carrying on the business is started, the business must be said to have commenced.*

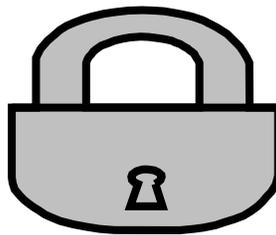
In this case it was held, on facts, that since the business had not commenced, the interest income could not be treated as business income. It was also held that the assessee was not entitled to the deduction of the administrative expenses and exploration and mining expenses from out of its interest income.

Income pending setting up of business : It is possible that pending setting up of business the funds raised by a company may be invested temporarily so that they do not remain idle. Income from such investments are taxable under income from other sources'. Expenses pending setting up of business like salary to staff, office expenses etc. cannot be deducted from such investment income [*Traco Cable Co. Ltd. v. CIT* (1969) 72 ITR 503 (Ker.)]. Companies in such a scenario are in an unenviable position. On the one hand they are incurring expenses which go a begging and on the other, they have income from investments which are taxed. The Madras High Court in *CIT v. Seshasayee Paper & Boards Ltd.* (1985) 156 ITR 542 (Mad.)] held that set off under Section 72 of the Act is also not possible because the expenses on business if they are not allowable as a deduction, cannot assume the form of loss either so as to qualify for set off against income from investments. Companies may therefore expedite setting up of business so that the business loss may be set off against such income from other sources.

It may be noted that the view expounded by the Madras High Court in *Seshasayee* (supra) has been endorsed by the Supreme Court in *Tuticornn Alkale Chemicals & Fertilisers Ltd. v. CIT* (1997) 27 CLA 41. In a subsequent judgement *CIT v. Bokare Steel Ltd.* (1999) 33 CLA (Sur.) 18, however the Supreme Court has pointed out that where it is possible to establish a link between investment income pending commencement of business with the cost of project, the same can be reduced from the cost of assets it has in fact gone to subsidise.

LESSON ROUND UP

- “Tax Planning may be legitimate provided it is within the framework of the law. Colorable devices cannot be part of tax planning and it is wrong to encourage or entertain the belief that it is honorable to avoid payment of tax by resorting to dubious methods.”
- Tax planning, in fact, is an honest and rightful approach to the attainment of maximum benefits of the taxation laws within their framework.
- The basic objectives of tax planning are: (a) Reduction of tax liability (b) Minimisation of litigation (c) Productive investment (d) Healthy growth of economy (e) Economic stability.
- “Tax Avoidance” will be used to describe every attempt by legal means to prevent or reduce tax liability which would otherwise be incurred by taking advantage of some provisions or lack of provisions of law. It excludes fraud, concealment or other illegal measures.
- Tax evasion is a method of evading tax liability by dishonest means like suppression, showing lower incomes, conscious violation of rules, inflation of expenses etc.

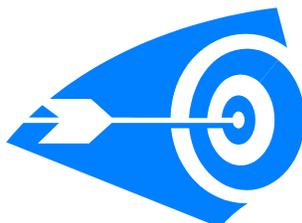
SELF-TEST QUESTIONS

1. Explain the concept of tax planning and state its importance for a company.
2. (a) Explain the three methods by which an assessee can reduce his tax liability.
(b) Distinguish between tax evasion and tax avoidance?
3. Explain the two schools of thought on tax avoidance. Enumerate the general principles regarding tax avoidance.

4. What are the objectives of tax planning? Enumerate the requisites for its success.
 5. Discuss in detail the areas where the tax planning can be resorted to by an assessee.
 6. Compare the different forms of organisation from tax liability points of view.
 7. Explain the significance of judicial pronouncements, notifications and circulars in the context of tax planning and outline the statutory force of notifications, circulars and rules framed by the Central Board for Direct Taxes.
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STUDY IV
TAX MANAGEMENT

LEARNING OBJECTIVES



The objective of the study lesson is to enable the students to understand:

- Filing of Income-tax Returns
- Defaults and Penalties
- Appeals and Revisions
- Alternate Dispute Resolution Mechanism

4.1 INTRODUCTION

The objectives of tax management are to ensure compliance with tax laws at the specified time and in the specified manner as also to ensure that the tax cost is minimized. The functions of tax management include tax planning, organizing the personnel to ensure tax compliance and directing and coordinating the compliance with all the provisions of tax laws.

In this study we will discuss various issues involved in tax management of an assessee covering the areas such as deduction of tax at source, advance payment of tax, filing of Returns of Income, appeals, revisions, filing application before Central Board of Direct Taxes under various sections of the Income Tax Act, 1961, defaults, interests and penalties. In this study we will also discuss the compliances prescribed under the Income Tax Act, 1961 such as maintenance of proper income-tax records, statements, charts, diagrams, tax deduction certificate, documents and papers required for filling the Income-tax Returns etc.

4.2 FILING OF INCOME-TAX RETURNS

Where the assessee is a company, it has to furnish return of its income in the prescribed form and certified in the prescribed manner and setting forth the prescribed particulars by 30th September of the assessment year. It is, therefore, essential for tax manager to ensure that all the requisite steps are taken duly in time. He must impress upon the auditors too to complete the audit well in time so that the statements of accounts can be prepared and approved well on time.

(A) MANDATORY FILING OF RETURN BY A COMPANY OR A FIRM

As per the provisions of Section 139 (1) of the Income Tax Act, 1961, every Company or a firm has to file its return of income as per Income Tax Rules. As per the Finance Act, 2001, w.e.f. Assessment Year 2001-02 it is mandatory for a Company or a firm to file a Return even if there is a loss or nil income. The return of

income is required to be filed on or before the due date which is 30th September of the assessment year in case of company assessee.

With retrospective effect from Assessment Year 2012-13, section 139 has been amended to provide that in case of all assesses who are required to obtain and file Transfer Pricing report as per Section 92E of the Act, the due date would be 30th November of the assessment year.

(B) LOSS CANNOT BE CARRIED FORWARD IF RETURN IS NOT FILED WITHIN THE PRESCRIBED TIME LIMIT

In cases where the assessee has sustained a loss in any previous year, under the head “profits and gains of business or profession” or “capital gains” and claims carry forward thereof, he has to file a return of loss in the prescribed form and manner and verified in the prescribed manner [Section 139(3)]. If return is not filed in time then loss will not be carried forward and set off.

(C) BELATED RETURN [SECTION 139(4)]

If the assessee has not furnished a return by 30th September or within the time specified under a notice issued by the Assessing Officer, the assessee may furnish the return for any previous year at any time before the expiry of one year from the end of the relevant assessment year or before the completion of the assessment whichever is earlier.

(D) REVISED RETURN [SECTION 139(5)]

The assessee is also permitted to furnish a revised return at any time before the expiry of one year from the end of the relevant assessment year or before the completion of the assessment (whichever is earlier) if he discovers any omission or wrong statement therein. Once a revised return is filed, the originally filed return must be taken to have been withdrawn and substituted by revised return. [*Dhampur Sugar Mills Limited v. CIT* (1973) 90 ITR 236 (All)]. A belated return i.e. return filed after the due date cannot be revised. Further, an assessee can file as many revised returns within the prescribed time limit.

(E) POWER OF BOARD OF DISPENSE WITH FURNISHING OF DOCUMENTS [SECTION 139C]

Section 139C has been inserted with effect from June 1, 2006. It provides that the Board may make rules providing for a class or classes of reasons who may not be required to furnish documents, statements, receipts, certificates, reports of audit or any other documents, which are otherwise under any other provisions of this Act, except Section 139D, required to be furnished, along with the return. However, such documents shall be produced on demand before the Assessing Officer.

(F) FILING OF RETURN IN ELECTRONIC FORM [SECTION 139D]

Section 139D has been inserted with effect from June 1, 2006. It provides that the Board may make rules providing for a class or classes of persons who shall be required of furnish the return of income in electronic form. The form and manner in

which the return of income in electronic form may be furnished; the documents, statements, receipts, certificates or audited reports which may not be furnished along with the return of income in electronic form but shall be produced before the Assessing Officer on demand. The computer resource or electronic record to which the return of income in electronic form may be transmitted.

(G) DEFECTIVE RETURN

The assessee has to ensure that the return is complete in all respects as otherwise the return is regarded as defective and invalid. A return is said to be defective if it is not complete in all respects and not duly filled in and in particular, must be accompanied by all the necessary annexures, statements, computation of tax payable on the basis of the return, audit report under Section 44AB; proof of payment of tax deducted at source, advance tax; statements of account, duly audited. Where the Assessing Officer considers the return defective, he may intimate defect to the assessee and give him an opportunity to rectify the defect within a period of 15 days which can also be extended on an application made by the assessee. If the defect is not rectified within the time allowed, the return shall be considered invalid and the assessee is deemed to have never furnished the return of his income at all and becomes liable to all penal provisions of the Income-tax Act.

(H) SIGNING OF RETURN (SECTION 140)

The return of income has to be signed by the Managing Director in the case of the company and in his absence by one of the Directors. In case a company is being wound up, the Return has to be signed by the Liquidator and in case of company whose management has been taken over by the Central Government or the State Government, by the principal officer thereof. If a company is a non-resident, the Return must be signed and verified by the person who is holding valid power of attorney for the purpose.

4.3 DEFAULTS AND PENALTIES

An assessee should note that compliance with legal formalities is less costly than the payment of penalties or interest on tax dues. There are several formalities to be complied with to avoid any penalty. In this connection, reference may be made to the following table summarising the defaults and penalties therefor.

The various types of penalties are briefly described in the table given below:

Section	Type of Default	Quantum of Penalty		Levied by (Authority)
		Minimum Penalty	Maximum Penalty	
1	2	3	4	5
140A(3)	Failure to pay the self assessment tax or interest or part thereof or both under Section 140A(1)	Such amount as the Assessing Officer may impose	Tax in arrears	Assessing Officer

1	2	3	4	5
158BFA	Determination of undisclosed income of block period	Minimum 100% of tax leviable in respect of undisclosed income	Maximum 300% of tax leviable in respect of undisclosed income	Assessing Officer or Commissioner (Appeals)
221(1)	Failure to make payment of tax and interest payable under Section 220(2) within the prescribed time limit	Such amount as the Assessing Officer may impose	Tax in arrears	- do -
271(1)(b)	Failure to comply with: (i) a notice under Sections 115WD(2); 115WE; 142(1); 143(2) or, (ii) a direction under Section 142(2A)	₹ 10,000 per failure	₹ 10,000 per failure	Assessing Officer
271(1)(c)	Concealment of the particulars of income or furnishing of inaccurate particulars of income	100% of tax sought to be evaded	300% of the amount of tax sought to be evaded	Assessing Officer or Commissioner (Appeals)
271(1)(d)	Concealment of particulars of Fringe Benefit	-do-	-do-	-do-
271(4)	Distribution of profit by registered firm otherwise than in accordance with partnership deed and as a result of which partner has returned income below the real income	Upto 150% of difference between tax on partner's income assessed and tax on returned income in addition to tax payable	—	-do-
271A	Failure to keep, maintain or retain books of account etc. as required under Section 44AA	₹ 25,000	₹ 25,000	Assessing Officer or Commissioner (Appeals)

1	2	3	4	5
271AA	Failure to keep and maintain information and document in respect of international transaction or specified domestic transaction or fails to report such transactions or maintains or furnishes an incorrect information or document .	—	A sum equal to 2% of the value of each international transaction or specified domestic transaction.	-do-
271B	Failure to get accounts audited under Section 44AB or furnish audit report along with return of income	One-half per cent of Total Sales, turnover	₹1,50,000	Assessing Officer
271BA	Failure to furnish report under Section 92E	₹ 1,00,000	—	-do-
271BB	Failure to subscribe to eligible issue of capital	20% of amount to be subscribed		
271C	Failure to deduct tax at source or failure to pay wholly or partly the tax u/s 115-O(2) or second proviso to Section 194-B	A sum equal to the amount of tax omitted to be deducted or paid	—	-do-
271CA	Failure to collect tax at source	100% of tax sought to be collected	—	Imposed by the Joint Commissioner
271D	Taking any loan or deposit in contravention of Section 269SS.	A sum equal to the amount of loan or deposit so taken or accepted	—	-do-

1	2	3	4	5
271E	Repayment of deposit in contravention of Section 269T.	A sum equal to the amount of deposit	—	-do-
271F	Failure to furnish returns as required by Section 139(1) and the proviso to Section 139(1) on or before due date	—	₹ 5,000	—
271FA	Failure to furnish Annual Information Return	₹ 100 per day for the days of default	—	—
271FB	Failure to furnish Fringe Benefit Return	₹ 100 per day for the days of default	—	—
271G	Failure to furnish information or document in respect of international transaction or specified domestic transaction under Section 92D(3).	A sum equal to 2% of the value of each international transaction or specified domestic transaction.	—	Assessing Officer or Commissioner (Appeals)
271H	Fails to furnish statement within the time prescribed in subsection (3) of section 200 or proviso to section 206C(3) or furnishes incorrect information. However, no penalty shall be payable if tax along with interest has been deposited and the statement has been furnished within one year from the time prescribed.	₹10,000	₹ 1,00,000	—
272A (1)(a)	Failure to answer any question put to person legally bound to state the truth of any matter touching the subject of his assessment by an income-tax authority.	—	₹10,000 for each default	Joint Director or Joint Commissioner

1	2	3	4	5
272A (1)(b)	Failure to sign any statement made by a person in course of income-tax proceeding	—	₹ 10,000 for each default	-do-
272A (1)(c)	Failure in compliance with summons issued under Section 131(1) to attend office to give evidence and produce books of accounts or other documents	—	₹ 10,000 for each default	Joint Director or Joint Commissioner
272A(2)	Failure to comply with a notice issued under Section 94, to give notice of discontinuance of business/ profession under Section 176(3); fails to furnish returns/ statements specified in Sections 133, 206, 206C, or 285B; fails to allow inspection of (i) register mentioned in Section 134, or (ii) entry in such register, or (iii) allow copies thereof to be taken, fails to furnish return of income under Section 139(4A) or, fails to deliver declaration under Section 197A; fails to furnish certificate under Section 203 or section 206C, fails to deduct and pay tax under Section 226; fails to deduct or pay tax u/s 192(2C), fails to deliver a copy of declaration u/s 206C(1A); fails to deliver the copy of statement within the time specified u/s 200(3) or the proviso to	—	₹ 100 for every day of default	Joint Director or Joint Commissioner (Chief Commissioner or Commissioner in case of default under Section 197A)

1	2	3	4	5
	206C(3); fails to deliver within the time specified u/s 206A(1). However, no penalty shall be payable where statement required u/s 200(3) or proviso to section 206C(3) on or after 1 st July 2012.			
272AA	Failure in compliance with Section 133B	Any amount subject to a maximum of ₹ 1,000	₹ 1,000	Joint Commissioner/ Asstt Director/ Assessing Officer
272B	Failure to comply with Section 139A (PAN)	₹ 10,000	—	—
272BB	Failure in compliance with Section 230A	—	₹ 10,000	Assessing Officer
272BBB	Failure to comply with Section 206CA (TCAN)	₹ 10,000	—	—

4.4 APPEALS AND REVISIONS

4.4.1 Right of Appeal

The right of appeal must be given by express enactment in the Act. Therefore, in case there is no provision in the Act for filing an appeal regarding a particular matter, no appeal shall lie. The right of appeal arises where the taxpayer is aggrieved by the order passed by the income-tax authority. Where the Assessing Officer accepts the return filed by the tax payer and passes an order making no modification, an appeal does not lie against that order as the taxpayer cannot be said to be aggrieved of that order. Similarly, where an appellate authority accepts the contention of the taxpayer and allows the appeal, there is no further appeal by the assessee against that order.

4.4.2 Appellate Authorities

The assessee may prefer an appeal against the orders of the Assessing Officer to the Commissioner (Appeals), in accordance with the relevant provisions under Section 246 and appeal against the order of the Commissioner (Appeals) can be preferred by the Assessee or the Commissioner of Income Tax and such appeal lies with the Appellate Tribunal.

The Finance (No.2) Act, 1998 has amended the provisions regarding remedy against order of Tribunal. Where earlier the assessee or the CIT, if not satisfied with the order of Tribunal, could only request the Tribunal to refer that matter to the High Court. After 1.10.98 as provided by Finance (No.2) Act, 1998 the assessee or CIT if not satisfied with the order of the tribunal can appeal directly to the High Court, if High Court is satisfied that the case involve a substantial question of law. Also, if the assessee or Commissioner of Income-tax is not satisfied with the order passed by the High Court they may file an appeal against the order of the High Court to the Supreme Court. However, it should be noted that in the case of question of fact tribunal is the final & binding authority and its decision is final.

4.4.3 Appealable orders before Commissioner (Appeals) (Section 246A)

Any assessee aggrieved by any of the following orders may appeal to the Commissioner (Appeals):

- (a) against an order passed by a Joint Commissioner under Clause (ii) of Sub-section (3) of Section 115VP or an order against the assessee where he denies his liability to be assessed under the Income Tax Act, under Section 143(3) except an order passed in pursuance of directions of Dispute Resolution Panel or Section 144 where assessee object to the amount of income assessed or amount of tax determined or amount of loss computed or status under which he is assessed;
- (aa) an order of assessment under Sections 115WE or 115WF where the assessee being an employer objects to the value of fringe benefits assessed;
- (b) against an order of assessment, re-assessment or re-computation under Section 147 or Section 150;
- (ba) an order of assessment or reassessment under Section 153A;
- (c) against an order of rectification of mistake under Section 154 or Section 155 having effect of enhancing assessment or reducing refund or order refusing to allow claim made by assessee under these sections;
- (d) against an order under Section 163 treating the assessee as the agent of a non-resident;
- (e) against an order under Section 170(2) of 170(3) relating to succession of business otherwise on death;
- (f) against an order made under Section 171;
- (g) against an order under Section 185;
- (h) against an order under Section 237;
- (i) A person deemed to be an assessee in default for not collecting the whole or any part of tax or after collecting the tax, failing to pay the same, may appeal before Commissioner (Appeals) on or after April 1, 2007.
- (j) against an order imposing a penalty under Section 221, 271, 271A, 271F, 271FB, 272AA, Section 272, 272B, 272BB or Section 273;

- (k) against an order of assessment made by an assessing officer under clause (c) of Section 158BC, in respect of search initiated under Section 132 or books of account, other documents or any assets requisitioned under Section 132A;
- (l) against an order imposing a penalty under Sub-section (2) of Section 158BFA;
- (m) against an order imposing penalty under Section 271 B or Section 271 BB;
- (n) against an order made by a Joint Commissioner imposing a penalty under Section 271 C, Section 271 D or Section 271 E;
- (o) against an order made by a Joint Commissioner imposing a penalty under Section 272AA and by a Joint Commissioner or Joint Director under Section 279A;
- (p) against an order imposing a penalty under Chapter XXI of Income tax Act;
- (q) against an order made by an Assessing Officer other than a Joint Commissioner under the provisions of this Act, in case of specified person or classes of persons.

Where a person has deducted and paid tax in accordance with Section 195 and 200 in respect of any sum (other than interest) chargeable under the Act he is entitled to prefer an appeal under Section 248 to be declared not liable to deduct tax. In other words, the right to appeal under Section 248 is conditional and can be exercised only if tax is deducted at source and paid to the Government.

Section 248 has been substituted with effect from June 1, 2007. The modified version provides that where under an agreement or other arrangement, the tax deductible on any income (not being interest) under Section 195 is to be borne by the payer (i.e., "net of tax" arrangement) and such person having paid such tax to the credit of the Central Government, claims that no tax was required to be deducted on such income, he may appeal to the Commissioner (Appeals) for a declaration that no tax was deductible on such income.

4.4.4 Procedure for filing of appeal [Section 249(1)]

The appeal should be filed in the prescribed form and verified in the prescribed manner. In case of an appeal made to the Commissioner (Appeals) on or after the 1st day of October, 1998, it shall be accompanied by a fees irrespective of the date of initiation of the assessment proceedings. The rates of fees are as follows:

- ₹250 when the assessed income is one hundred thousand rupees or less (income/loss) compute.
- ₹ 500 when the assessed income is more than one hundred thousand rupees but not more than two hundred thousand rupees.
- ₹1000 when the assessed income is more than two hundred thousand rupees.
- ₹250 in any other case.

Form No. 35 is the prescribed form [under Rule 45(1)] of the appeal. The form of appeal, the grounds and the verification appended to the form should be signed [Rule 45(2)] as per provisions applicable to the signing of return under Section 140.

Form No.35 requires that the memorandum of appeal, statement of facts and the grounds of the appeal must be in duplicate and should be accompanied by a copy of the order appealed against and the notice of demand in original, if any.

4.4.5 Period of limitation to prefer an appeal [Section 249(2)]

The appeal has to be presented within the period of limitation as given below:

- 1. Appeal by person denying liability to deduct tax in respect of payments payable to non-resident or a foreign company [Section 249(2)(a)] :** Where the appeal relates to any tax deducted at source from payment made to a non-resident, (other than a company) or to a foreign company, any interest, other 'than interest on securities or any other sum chargeable under the provisions of the Income Tax Act (not being salaries), within 30 days from the date of payment of tax deducted at source to the credit of the Central Government.
- 2. Appeal against assessment to penalty [Section 249(2)(b)] :** Where the appeal relates to any assessment or penalty order the appeals have to be presented within 30 days of the date of service of the notice of demand relating to that assessment or penalty order.
- 3. Other appeals [Section 249(2)(c)] :** In any other case, the appeal has to be presented within 30 days of the date on which intimation of the order sought to be appealed against is served on the appellant.

In computing the period of limitation for an appeal or an application, the day on which the order is served has to be excluded. If the assessee was not furnished with a copy of the order along with the notice of the order, or demand, the time required for obtaining a copy of such order is also to be excluded and the date will be extended by that period. It may be noted that even where the assessee has not been supplied with copy of the order concerned, the time taken in making an application which does not comply with all the legal requirements cannot be excluded under the provisions of Section 268. If the application for obtaining the copy of the order has not been properly stamped or has been made by a person not authorised to do so, the time which has elapsed between the making of the invalid application and putting the application in order would not be excluded in computing the period of limitation.

If any appeal is filed after the period of limitation, the Commissioner (Appeals) may admit the appeal after the said period if he is satisfied that the appellant had sufficient cause for not presenting the appeal within that period [Section 249(3)]. Such delayed appeals must be accompanied by a condonation petition showing and explaining the reason/cause of the appellant for not being able to file the appeal within the period of limitation and praying for condemnation of the delay. The power to condone the delay is discretionary and the discretion must be judiciously exercised. The discretion is to be exercised where sufficient cause for not presenting the appeal within the time is made out by the appellant. The period for filing an appeal cannot be extended simply because the appellant's case is hard and calls for

sympathy or merely out of benevolence to the party seeking relief. The sufficient cause must be a cause which is beyond the control of the party seeking the condonation of the delay. Illness is sufficient cause, if it can be shown that the man was utterly disabled to attend to any duty. The cause for delay in filing the appeal which, by due care and attention could have been avoided cannot be a sufficient cause. Negligence on the part of the servants or agent entrusted with the filing of the appeal cannot be considered as a sufficient cause. The change of legal situation brought about by a decision of the Supreme Court may be valid ground for condoning delay. The words "sufficient cause" should receive a liberal interpretation so as to advance substantial justice where no negligence nor inaction nor want of bona fide is imputable to the applicant.

An appeal presented after the period of limitation is still an "appeal" and an order dismissing it as time barred is one passed in appeal [under Section 250 and not under Section 249(3)]. An appeal lies therefrom to the Appellate Tribunal and thereafter to the High Court on a question of law.

Payment of Tax before Filing Appeal [Section 249(4)]

No appeal against any order passed by the Assessing Officer can be admitted by the Commissioner (Appeals) unless at the time of filing of the appeal the assessee has paid tax due on the income returned by him, and where the assessee has not furnished the return of income, he has paid an amount equal to the amount of advance tax which was payable by him. If the appellant wants exemption from the payment of such tax he has to make an application to the Commissioner (Appeals) who is empowered to waive this requirement in appropriate cases if he is satisfied that there are good and sufficient reasons for doing so. In such cases, the Commissioner (Appeals) is required to record such reasons in writing. It may be noted that Income-tax law requires only the payment of tax before the filing of the appeal and not the payment of any penalty or any other sum payable by the assessee on the basis of the order appealed against.

Procedure in appeal (Section 250)

Commissioner (Appeals) shall fix a day and place for the hearing of the appeal and shall give notice of the same to the appellant and to the Assessing Officer against whose order the appeal is preferred.

The following shall have the right to be heard at the hearing of the appeal:

- (a) The appellant, either in person or by an authorised representative.*
- (b) The Assessing Officer, either in person or by a representative.*

The Commissioner (Appeals) shall have the power to adjourn the hearing of the appeals from time to time. He may, before disposing of any appeal, make such further enquiry as he deems fit, or may direct the Assessing Officer to make further enquiry and report as he deems fit, or may direct the Assessing Officer to make further enquiry and report the result of the same to the Commissioner (Appeals).

The Commissioner (Appeals) may, at the hearing of an appeal, allow the appellant to go into any ground of appeal not specified in the grounds of appeal if he is satisfied that the omission of that ground from the form of appeal was not willful or

unreasonable. His order disposing of the appeal shall be in writing and shall state the points for determination, the decision thereon and the reasons for the decision. In every appeal, the Commissioner (Appeal), where it is possible, may hear and decide such appeal within a period of one year from the end of the financial year in which such appeal is filed before him Commissioner (Appeal) under Section 246A(1). On the disposal of the appeal, the Commissioner (Appeals) shall communicate the order passed by him to the assessee and to the Chief Commissioner or Commissioner.

Powers of the Commissioner (Appeals) (Section 251)

In disposing of an appeal, the Commissioner (Appeals) shall have the following powers:

1. In an appeal against an order of assessment, he may confirm, reduce, enhance or annul the assessment.
2. In an appeal against an order imposing a penalty, he may confirm or cancel such order or vary it so as to either enhance or reduce the penalty.
3. In any other case, he may pass such orders in the appeal as he deems fit.

The Commissioner (Appeals) shall not enhance an assessment or a penalty or reduce the amount of refund unless the appellant has had a reasonable opportunity of showing cause against such enhancement or reduction.

While disposing an appeal, the Commissioner (Appeals) may consider and decide the facts arising out of the proceedings which in respect of order appealed against were carried notwithstanding that such matter was not raised before the Commissioner (Appeals) by the appellant.

From the Assessment year 2009-10, in an appeal against the order of assessment in respect of which the proceedings before the Settlement Commission abates under the section 245HA, the Commissioner (appeals) can confirm, reduce, enhance or annul the assessment after taking into consideration of the following –

1. *the material and other information produced by the assessee before the Settlement Commission*
2. *the results of the enquiry held by the Settlement Commission*
3. *the evidence recorded by the Settlement commission in the course of proceedings before it*
4. *such other material as may be brought on his record.*

4.4.6 Revision by the Commissioner of Income Tax (Sections 263 and 264)

The right to file such appeals against the orders of the Assessing Officer is not available to the Department. It is for this reason that the Commissioner has been vested with revisional powers under Section 263, where the order of the Assessing Officer is erroneous in so far as it is prejudicial to the interests of the revenue. But such revisional power can be exercised only in respect of orders which are not the subject matter of appeals. The reason is that once an assessment order is appealed against, the Commissioner (Appeals) has got the powers to enhance the assessment under Section 263 and a right of appeal upto the Tribunal is provided to the assessee

against the orders of the Assessing Officer. In the following cases Commissioner of Income-tax can revise an order passed by the Assessing Officer:

4.4.7 Revision of orders prejudicial to the interest of revenue (Section 263)

The Department has no right of appeal to the Commissioner (Appeals) against any order passed by the Assessing Officer. Therefore, the Commissioner of Income-tax has been empowered to revise such orders of the Assessing Officer as are prejudicial to the interest of the revenue. Such power, however, is subject to certain conditions as given below :

1. ***Revision can be only of the order of Assessing Officer [Section 263(1)]***: The Commissioner of Income-tax can revise only the orders of Assessing Officer. For the purposes of this clause, an order passed by the Assessing Officer includes an order of assessment passed on or before or after 1.6.1988, including: (i) an assessment order made by the Assistant Commissioner or the Income Tax Officer on the basis of the directions issued by the Joint Commissioner under Section 144A, (ii) an order made by the Joint Commissioner in exercise of the powers or in performance of the functions of an Assessing Officer conferred on, or assigned to him under the orders or directions issued by the Board or by the Chief Commissioner or Director General or Commissioner authorised by the Board in this behalf under Section 120 [Jurisdiction of Income Tax authorities].

In case the order referred to above has been the subject matter of any appeal filed on or before or after June 1, 1988 the powers of the Commissioner shall extend and shall always be deemed to have extended to such matters as had not been considered and decided in such appeal. The appellate orders passed by the Commissioner (Appeals) are outside the purview of the revisional powers vested in the Commissioner of Income-tax. But if the assessment order of the Assessing Officer is pending in an appeal before the appellate authority (as aforesaid), it can be revised by the Commissioner of Income-tax. So long the appeal is not disposed of, the order of the Assessing Officer will be considered as subsisting and operative. Therefore, it can be revised.

2. ***Order erroneous and prejudicial to the interest of revenue [Section 263(1)]*** : If the Commissioner of Income-tax considers that the order of the Assessing Officer is erroneous in so far as it is prejudicial to the interest of the revenue, such order can be revised after giving the assessee an opportunity of being heard.

The word "erroneous" includes cases where there has been a failure to make the necessary enquiries. The Commissioner of Income-tax may consider an order of the Assessing Officer to be erroneous not only if it contains some apparent error of reasoning or of law or of fact on the face of it but also because it is a stereotype order which simply accepts what the assessee has stated in his return and fails to make enquiries which are called for in the circumstances of the case. The Assessing Officer is not only an adjudicator but also an investigator. He cannot remain passive in the face of a return which is apparently in order but calls for further enquiry. It is

his duty to ascertain the truth of the facts stated in return when the circumstances of the case are such as to provoke enquiry.

The words “prejudicial to the interests of revenue” appearing under Section 263(1) have not been defined in the Act, but they must mean that the order of the Assessing Officer is such, that it is not in accordance with law in consequence whereof the lawful revenue due to the State has not been realised or cannot be realised. The Allahabad High Courts’ decision in *Commissioner of Income-tax v. Sunder Lal* (1974, 96 ITR 310) was followed by it in *Commissioner of Income-tax v. Kashi Nath & Co.* 1988, 170 ITR 28) holding that the power of the Commissioner of income-tax under Section 263 of the Income Tax Act is quasi-judicial in character. He must give reasons in support of his conclusion that the assessment order is erroneous in so far as it is prejudicial to the interests of the Revenue. If he does not give the reasons, the order can be vitiated. For example, if the Commissioner is of the opinion that the Assessing Officer had allowed deductions in excess of what they were due in a particular case, such order is erroneous and prejudicial to the interests of the revenue. Hence, it may be revised by the Commissioner of Income Tax.

In *Malabar Industrial Co. Ltd. v. Commissioner Income Tax* (1992, 198 ITR 611) the Kerala High Court held that the words ‘prejudicial to the interests of the revenue’ are of wide import and they should not be limited to a case where the order passed by the Income-tax Officer (now Assessing Officer) can be considered to be one prejudicial to the revenue administration as such. The question whether an order of the Income Tax Officer is prejudicial to the interests of revenue would depend on the facts of each case and there can be no universal formula applicable to finding out any such prejudicial error. The High Court followed the rule laid down by the Supreme Court in *Tara Devi Aggarwal v. CIT* (1973, 88 ITR 523) but dissented from the rule laid down by the Madras High Court in *Venkatakrishna Rice Co. v. CIT* (1987, 163 ITR 129).

The Commissioner can revise an order passed by the Assessing Officer only if it is erroneous and prejudicial to the interests of the revenue; if the order sought to be revised is not prejudicial to the interest of the revenue the Commissioner has no jurisdiction to revise it. The failure of the Assessing Officer to deal with the claim of the assessee in the assessment order may be an error, but an erroneous order by itself is not enough to give jurisdiction to the Commissioner to revise it under Section 263. It must be further shown that the order was prejudicial to the interests of the revenue.

3. Assessee to be given an opportunity of being heard [Section 263(1)] :

The process of revision is completed in three stages: (i) the Commissioner may call for and examine the records of any proceeding under the Act which is within his administrative powers. If after examining the material and relevant facts on record, the Commissioner considers prima facie that any order of the Assessing Officer is erroneous and prejudicial to the interest of the revenue, he must, in the (ii) place, give the assessee an opportunity of being heard. The opportunity of being heard to be given to the assessee contemplates that the Commissioner must disclose to the assessee the grounds on which he desires to make a revision under Section 263. This is

essential. If the assessee does not know on what points he is to be heard, he may not visualise what he has to say at the hearing and the opportunity of being heard may prove to be illusory. Further, the notice to show cause must be served on the assessee reasonably ahead of the date fixed for hearing, because the time allowed to the assessee to prepare the case should not be short but reasonable. The Commissioner is also required to examine the merits of the objection raised by the assessee. Without going into the merits of the claim of the assessee, it is not possible for the Commissioner to say that the order of the Assessing Officer has caused any prejudice to the interests of the revenue. He may also cause enquiry to be made by his subordinates. Before making his order, he must disclose to the assessee the material collected by him on enquiry if he wants to use the materials collected from such inquiry against the assessee. If the matter collected from the enquiry is only supporting material and does not constitute the basic grounds on which the revision order is to be passed, the failure of the Commissioner to disclose to the assessee the fact of the enquiry does not vitiate the revision order.

In the third stage, the Commissioner is required to pass the necessary order if he finally concludes that the order of the Assessing Officer is erroneous and prejudicial to the interests of the revenue. He can enhance or modify the assessment. He has also the power to cancel the assessment and direct a fresh assessment. The power of cancellation of the assessment with a direction to make a fresh assessment is called for only in cases where there is something totally or basically wrong with the assessment which is not capable of being remedied by amendments to the assessment order itself. Where the Commissioner comes to the conclusion that there is a defect in the assessment order in so far as the question of the levy of interest was not considered by the Assessing Officer, the Commissioner should direct the Assessing Officer to consider the question on merits and in accordance with law after giving the assessee an opportunity of being heard. It is not further necessary for him, nor would the circumstances of the case justify, that the whole assessment should be set aside. Setting aside the assessment has got far reaching consequences and such power should be exercised only where the circumstances call for a remedial action. The revisional order must be a speaking order giving reasons for such revisions otherwise the order may be vitiated. The power of suo-moto revision of the Commissioner of Income-tax under Section 263(1) is in the nature of supervisory jurisdiction and can be exercised only if the circumstances specified therein exist. Two circumstances must exist: (i) the order should be erroneous, and (ii) by virtue of the order being erroneous, prejudice must have been caused to the interests of the revenue. An order cannot be termed as erroneous unless it is not in accordance with law. If an Income-tax Officer acting in accordance with law makes certain assessment, the same cannot be termed as erroneous by the Commissioner simply because according to him, the order should have been written more elaborately. In this case, the Tribunal was held justified in setting aside the order passed by the Commissioner under Section 263.

4. ***Time limit for making the revisional order [Sections 263(2) and (3)] :***
The revisional order can be passed within two years from the end of the

financial year in which the order sought to be revised was passed [Section 263(2)]. Once the revisional order is made within the time limit of two years from the end of the relevant financial year it is a valid order even if it is served on the assessee after the expiry of two years.

In computing the time limit of two years, the time taken in giving an opportunity to the assessee to be reheard (under Section 129) and any period during which the proceeding (under Section 263) is stayed by an order or injunction of any court is excluded [Explanation to Section 263(2)]. Order under Section 263 can't be passed to reduce tax utility or in favour of assessee. However Appeal against Section 263 can be made to ITAT.

It may be noted that the limit of two years does not apply to a revisional order which had been passed in consequences of or to give effect to, any finding or direction contained in an order of the Appellate Tribunal, the High Court or the Supreme Court. Such revisional order may be passed at any time [Section 263(3)].

4.4.8 Revision of order in the Interest of Assessee (Section 264)

An aggrieved assessee has his normal right of appeal against the order of the Assessing Officer to Commissioner (Appeals) under Section 246A and thereafter to the Appellate Tribunal under Section 253. Further, each and every order of the Assessing Officer is not appealable to the appellate authorities under Sections 246A and 253. The assessee may seek justice in such cases by making an application under section 264 to the Commissioner of Income Tax. For example, revision lies to the Commissioner against the levy of penal interest for not furnishing the return of total income within the prescribed time against which no appeal has been provided.

The revisional order passed under Section 264 cannot be prejudicial to the interest of the assessee. The whole subject matter is discussed below —

- 1. Revision of order of subordinate authority only [Section 264(1) and Explanation 2] :** The Commissioner of Income Tax may revise any order of an authority subordinate to him. Deputy Commissioner, Income Tax Officers and Inspectors of Income Tax are subordinate to the Commissioner according to Section 118.
- 2. Suo motu revision [Section 264(1) and (2)] :** The Commissioner may, *suo motu* call for the record of any proceeding under this Act in which any, order has been passed by any authority subordinate to him. He may make such enquiry and may pass such order as he thinks fit but such order cannot be prejudicial to the assessee [Section 264(1)]. He may act in such circumstances without notice to the assessee and without giving him an opportunity of being heard. Such exercise of the authority is a purely departmental affair and the assessee may know nothing about this. While acting *suo motu*, the Commissioner may revise the order of his subordinate authority within one year from the date of the order sought to be revised [Section 264(2)]. If the order has been made more than one year back, such order cannot be revised by him.

It is obligatory on the Commissioner w.e.f. October 1, 1998 to pass an order under Section 264 within a period of one year from the end of financial year in which the application is made for revision. In computing the period of

limitation, the time taken in giving an opportunity to the assessee to be re-heard (under Section 129) and any period during which any proceeding under this Section is stayed by an order or injunction of any court is excluded. Though an order has, to be passed within one year, an order in revision may be passed at any time in consequence of or to give effect to any findings or directions contained in an order of the Appellate Tribunal, High Court or the Supreme Court.

- 3. Revision on application of the assessee [Section 264(1), (3) & (5)] :** The assessee is entitled to make an application to the Commissioner of Income-tax for the revision of any order passed by an authority subordinate to him. Such an application can be made within one year from the date on which the order in question was communicated to him or from the date on which he otherwise came to know of it, whichever is earlier [Section 264(3)]. The Commissioner is empowered to admit a belated application if he is satisfied that the assessee was prevented by sufficient cause from making the application within the prescribed time.

The application for revision by the assessee is always to be accompanied by a fee of ₹500 [Section 264(5)]. On receipt of the revision application, the Commissioner may call for the record. He may make such enquiry and pass such order as he deems fit. Such an order should not be prejudicial to the assessee [Section 264(1)].

There are two important points of distinction between the cases: (i) where the Commissioner makes suo motu revision; and (ii) where he makes a revision on the application of the assessee. While acting suo motu, he can pass the revisional order only within one year from the date of the order sought to be revised. There is no such time limit when the revisional order is passed on the basis of application filed by the assessee. Once the application is made within the period of limitation prescribed therefor, or after the condonation of delay, the order may be passed at any time thereafter. Secondly, while acting suo motu, the Commissioner acts in the exercise of his administrative jurisdiction and, hence, he is not bound to give a hearing to the assessee. In fact the review is purely a departmental affair in such cases. On the other hand, when he is moved by the assessee for the said purposes, the jurisdiction conferred on him is a judicial one and, hence, he must give an opportunity to the assessee to put forward his case.

- 4. Nature of the order under Section 264 :** The Commissioner may pass such order as he thinks fit provided such order is not prejudicial to the assessee. This is so whether the Commissioner acts suo motu, or on the revision application of the assessee. An order of the Commissioner passed in revision can be said to be prejudicial to the assessee only when he is, as a result of it, placed in a different and worse position than that in which he was placed by the order under review'. If the Commissioner effects a reduction of income under one head and an increase under another but, on the whole reduces the assessment, his order cannot be said to be prejudicial to the assessee. Though the Commissioner may not change the order of the subordinate authority to the prejudice of the assessee, he may not give the relief asked for by the assessee. An order of the Commissioner

declining to interfere with the order of the subordinate authority cannot be deemed to be an order prejudicial to the assessee (Explanation 1 to Section 264). The power to pass such orders as he deems fit is not an arbitrary one to be exercised according to his fancy. He must act according to the rules of reason and justice, not according to private opinion, according to law not humor. His discretion is not to be arbitrary, vague and fanciful, but legal and regular. It is a power coupled with duty to exercise it in the interest of justice to the assessee.

5. *Circumstances in which no revision can be made [Section 264(4)]* : The Commissioner of Income-tax cannot revise the order of his subordinate authority in the following cases:

- (i) If the order is appealable to the Commissioner (Appeals), such order cannot be revised until the time within which such appeal may be made expires. If an appeal has been made to the Commissioner (Appeals), the revisional power cannot be exercised while the appeal is pending but it may be exercised after the appeal has been disposed of. The Commissioner (Appeals) for the purpose of Section 264 is an authority subordinate to the Commissioner of Income-tax. Hence, the order of the Commissioner (Appeals) can be revised.
- (ii) If the order is appealable to the Commissioner (Appeals) or the Appellate Tribunal, revisional power cannot be exercised until the time within which such appeal may be made expires. But, in such cases, if the assessee waives his right of appeal, the Commissioner may revise the order even before the time for appeal has expired. But once the order has been made the subject of an appeal the revisional powers come to an end. An order can be said to be made the "subject of an appeal" only when it is the subject of an effective appeal. If the Commissioner (Appeals) or the Appellate Tribunal refuses to entertain an appeal on the ground that it is time barred, or grants permission to the appellant to withdraw the appeal, the order cannot be said to be the "subject of an appeal" and the assessee would be entitled to apply to the Commissioner for revision.

4.4.9 Remedy against the revisional order

An order of the Commissioner passed under Section 264 is not appealable to the Tribunal. Nor does a reference lie against such an order to the High Court since a reference to the High Court lies only against an order passed by the Tribunal. Since the order of the Commissioner is judicial or quasi-judicial in character, it is within the ambit of the High Court's jurisdiction under Article 226 of the Constitution and a petition for a writ of certiorari to quash an unjust or illegal order of the Commissioner is maintainable.

4.5 APPELLATE TRIBUNAL (SECTION 252)

The Central Government shall constitute an Appellate Tribunal consisting of as many judicial and accountant members as it thinks fit to exercise the powers and discharge the functions conferred on the Appellate Tribunal by this Act. The ITAT is constituted and works under the Ministry of Law. It is thus a body outside the administrative control of the Central Board of Direct Taxes.

The Appellate Tribunal is not an Income-tax Authority in the sense of being an integral part of the department. On the contrary, by its constitution, powers and jurisdiction, not to speak of the manner of their recruitment, the Tribunal is an independent arbitral tribunal. The proceedings before it are advisory. It has also the trappings of a judicial body in the sense that it has to deal with the Department on the one side, and the assessee on the other in as much as they face each other as opposing parties. In such a situation the Tribunal has to decide only those issues which are properly raised before it by the one or the other party in the appeal or in the cross objections. Under the Act, the Tribunal has got to decide an appeal and not merely give it a disposal by dismissing it for default of appearance. This, however, does not mean that the Tribunal has got to take upon themselves the responsibility of finding facts or points of law which are not urged by the Department or the assessee, as the case may be. *CIT v. A. C. Paul* (1983) 142 ITA 811 (Mad.).

The Tribunal is the final Authority and ordinarily, if after considering the matters in the proper perspective and after surveying all material which is available to it, the Tribunal arrives at some conclusion one way or the other, that conclusion would have to be respected, unless it can be regarded as impossible or perverse. *CIT v. Lalchand Bhabutmal Jain* (1985) 151 ITR 360 (Bom.).

Appealable orders [Section 253(1) and (2)] : Any assessee aggrieved by any of the following orders may appeal to the Appellate Tribunal against such order.

1. An order passed by Commissioner (Appeals) under Section 154 ordering a rectification of mistake, or under Section 250 in connection with the disposal of an appeal or Section 271 imposing a penalty for failure to furnish return etc. or Sections 271 A or 272A.
2. An order passed by an assessing officer under Clause (c) of Section 158BC, in respect of search initiated under Section 132 or books of account other documents or any assets requisitioned under Section 132A, after the 30th day of June, 1995 but before the 1st day of January, 1997.
3. An order passed by a Commissioner under Section 12AA relating to registration of trust or under Section 263 relating to revision of orders prejudicial to revenue or under Section 272A penalty for failure to answer question, sign statements, allow inspection etc., on or under Section 154 rectifying a mistake, or an order passed by a Chief Commissioner, or a Director General or a director under Section 272A.
4. An order passed by an Assessing Officer under Sub-section (1) of Section 115VZC.
5. An order passed by a Commissioner for rejection of approval under Section 80G(5)(vi).

The Commissioner may, if he objects to any order passed by Commissioner (Appeals) under Section 154 or 250, direct the Assessing Officer to appeal to the Appellate Tribunal against the order.

Procedure for filing appeal [Section 253(3), (4)&(6)] : Every appeal to the Appellate Tribunal shall be filed within sixty days of the date on which the order sought to be appealed against is communicated to the assessee or to the Commissioner, as the case may be.

The Assessing Officer or the assessee, as the case may be, on receipt of notice that an appeal against the order of the Commissioner (Appeals) has been preferred by the other party may, notwithstanding that he may not have appealed against such order or any part thereof, within thirty days of the receipt of notice, file a memorandum of cross-objections, verified in the prescribed manner, against any part of the order of the Commissioner (Appeals) and such memorandum shall be disposed of by the Appellate Tribunal as if it were an appeal presented within the specified period.

The Appellate Tribunal may admit an appeal or permit the filing of a memorandum of cross-objections after the expiry of the relevant period if it is satisfied that there was sufficient cause for not presenting it within that period.

An appeal to the Appellate Tribunal shall be in the prescribed form and shall be verified in the prescribed manner and shall, in case of an appeal made on or after the 1st day of October, 1998, irrespective of the date of initiation of the assessment proceedings be accompanied by a fine of :

- (a) ₹ 500 where the assessed income/loss is 1,00,000 rupees or less.
- (b) ₹ 1,500 where the assessed income/loss is more than one hundred thousand rupees but not more than two hundred thousand rupees.
- (c) One percent of the assessed income, subject to a maximum of ten thousand rupees where the assessed income is more than two hundred thousand rupees,
- (d) ₹ 500 in any other case, except in case of an appeal filed by the department or a memorandum of cross-objections.

An application for stay of demand has to be accompanied by a fee of ₹ 500.

In making an appeal to the Tribunal, the following documents shall be sent in triplicate.

- (a) *The memorandum of appeal.*
- (b) *The grounds of appeal.*
- (c) *Copy of the order of the Commissioner (Appeals).*
- (d) *Copy of the grounds of appeal and statement of facts filed before the Commissioner (Appeals).*
- (e) *Copy of the order of the Assessing Officer.*
- (f) *Challan for payment of requisite fee.*

Where the appellant desires to refer to any documents or evidence he is permitted to file the same with Tribunal in the form of a paper book within one month from the date of filing the appeal. Though the prescribed period is one month, it will be preferable to file the same along with the appeal. Where an appellate order by the Commissioner (Appeals) is passed as a consolidated order for a number of years, appeals to the Tribunal shall be filed separately for each year.

Order of Appellate Tribunal (Section 254) : The Appellate Tribunal may, after

giving both the parties to appeal an opportunity of being heard, pass such orders thereon as it may think fit.

The Appellate Tribunal may, at any time within four years from the date of the order, with a view to rectifying any mistake apparent from the record, amend any order passed by it and shall make such amendment if the mistake is brought to its notice by the assessee or the Assessing Officer. But, any amendment which has the effect of enhancing an assessment or reducing a refund or otherwise increasing the liability of the assessee shall not be made unless the Appellate Tribunal has given notice to the assessee of its intention to do so and has allowed the assessee a reasonable opportunity of being heard.

The Tribunal's decision would have binding effect within the jurisdiction and has a persuasive value outside its jurisdiction.

Sub-sections (2A) and (2B) have been inserted by Finance Act, 1999 w.e.f. 1.6.99. Sub-section (2A) provides that in every appeal, the Appellate Tribunal, where it is possible may hear and decide such appeal within a period of four years from the end of the financial year in which such appeal is filed under Section 253(1). Sub-section (2B) provides that the cost of any appeal to the Appellate Tribunal shall be at the discretion of the Tribunal.

Section 254(2A) pertaining to stay of demand by the Appellate Tribunal has been modified as follows:

1. Initially the Tribunal can pass an order of the stay only for a period not exceeding 180 days from the date of the order staying the demand.
2. The tribunal shall dispose of appeal within the aforesaid period.
3. If appeal is not disposed of within the aforesaid period, the period of stay may be extended. The total period of stay cannot be more than 365 days reckoned from the beginning of the period. Extension is possible only if delay is not attributable to assessee.
4. Appeal shall be disposed of by the Tribunal within the extended period.
5. If appeal is not disposed of within the extended period or periods, the order of stay shall stand vacated after the expiry of such period or periods.

The Appellate Tribunal shall send a copy of any orders passed under this section to the assessee and to the Commissioner. On question of fact, the order passed by the Appellate Tribunal on appeal shall be final. An order made by the Appellate Tribunal shall be sufficiently comprehensive and self-contained. It should be possible to ascertain from the order all the relevant facts and the questions arising on the appeal. It should also disclose what were the contentions of the parties and should state why and for what reasons those contentions were repelled.

Under Section 254(1), the Tribunal may, after giving both parties to the appeal an opportunity of being heard, pass such-orders thereon as it deems fit.

No limitation has been placed on the powers of the Commissioner (Appeals) or the Appellate Tribunal under Section 251(1) or 254(1). The only limitation on their appellate jurisdiction is that they cannot go into the question of propriety of an ex-

parte proceeding or a best judgement assessment. The quantum of assessment, the quantum of tax or the question of registration of a firm can always be gone into. *Vishnu Kumar Gupta v. CIT* (1983) 143 ITR 169 (All). However, the power of stay is not likely to be exercised in a routine way or as a matter of course in view of the special nature of taxation and revenue laws. Only when a strong prima facie case is made out, the Tribunal will consider whether to stay the recovery proceedings. Stay will be granted only in deserving and appropriate cases and where the Tribunal is satisfied that the entire purpose of the appeal will be frustrated or rendered nugatory by allowing the recovery proceedings to continue during the dependency of the appeal before it.

Section 254(1) empowers the Appellate Tribunal to give its decision on the grounds urged and it can pass appropriate orders. It is not open to the Tribunal itself to raise a ground or permit the party who had not appealed to raise a ground which will work adversely on the appellants.

Under Section 254(2), the Appellate Tribunal has got ample power to rectify a mistake apparent from record *suo motu*. If the mistake is brought to the notice of the Tribunal by the parties to the appeal, the Tribunal is empowered to rectify the same. *Addl. CIT v. ITAT* (1983) 139 ITR 615 (AP).

From the Assessment year 2009-10(w.e.f.1.10.2008),the third proviso to sub-section (2A) provides that if such appeal is not decided within the period allowed originally or the periods so extended or allowed ,the order of stay shall stand vacated after expiry of such period or periods.

The intention behind these provisions has been very clear that the Appellate tribunal cannot grant stay either under the original order or any other subsequent order, beyond the period of 365 days in aggregate.

If the Tribunal is unable to decide the appeal on the basis of materials before it, it may admit fresh evidence and decide the appeal. It may also keep the appeal pending and direct any one of the subordinate authorities to ascertain further facts.

Procedure of Appellate Tribunal (Section 255) : The powers and functions of the Appellate Tribunal may be exercised and discharged by benches constituted by the President of the Appellate Tribunal from amongst the members thereof. The bench shall consist of one judicial member and one accountant member.

The President or any other member of the Appellate Tribunal, authorised in this behalf by the Central Government, may, sitting singly, dispose of any case which has been allotted to the Bench of which he is a member and which pertains to an assessee whose, total income as computed by the Assessing Officer in the case does not exceed ₹5,00,000. The President may, for the disposal of any particular case, constitute a Special Bench consisting of three or more members, one of whom shall necessarily be a judicial member and one an accountant member.

If the members of a Bench differ in opinion on any point, the point shall be decided according to the opinion of the majority if there is a majority. But if the members are equally divided, they shall state the point or points on which they differ and the case shall be referred by the President of the Appellate Tribunal for hearing on such point or points by one or more of the other members of the Appellate

Tribunal. Such point or points shall be decided according to the opinion of the majority of the members of the Appellate Tribunal who have heard the case including those who first heard it.

The Appellate Tribunal shall have the power to regulate its own procedure and the procedure of Benches thereof in all matters arising out of the exercise of its powers or of the discharge of its functions including the places at which the Benches shall hold their sittings.

The Appellate Tribunal shall have, for the purpose of discharging its functions, all the powers which are vested in the Income-tax authorities under Section 131, and any proceeding before the Appellate Tribunal shall be deemed to be a judicial proceeding and for the purpose of Section 196 of the Indian Penal Code, the Appellate Tribunal shall be deemed to be a Civil Court for all purposes of Section 195 and Chapter XXXV of the Code of Criminal Procedure.

The Appellate Tribunal is a final fact finding authority and if it arrives at its own conclusions or facts after the consideration of the evidence before it, the Court will not interfere. It is necessary, however, that every fact 'for' and 'against' the assessee must have been considered with due care and the Tribunal must have given its finding in a manner which would have clearly indicated what were the questions which arose for determination, what was the evidence pro and contra in regard to each one of them, and what were the findings reached on the evidence on record before it.

4.6 APPEAL TO HIGH COURT

Sections 260A and 260B are inserted w.e.f. October 1, 1998. Section 260A provides that an appeal shall lie to the High Court from every order passed in appeal by the Appellate Tribunal if the High Court is satisfied that the case involves a substantial question of law.

The Chief Commissioner or the Commissioner or an assessee aggrieved by any order passed by the Appellate Tribunal may file an appeal to the High Court and such appeal shall be filed within 120 days of the date on which the order appealed against is received by the assessee or the Chief Commissioner or Commissioner and shall be filed in the form of memorandum of appeal precisely stating the substantial question of law involved.

If the High Court is satisfied that a substantial question of law is involved in any case, it shall formulate that question. The appeal shall be heard only on the question so formulated, and the respondents shall at the hearing of the appeal, be allowed to argue that the case does not involve such question. However, the High Court may for reasons to be recorded, hear the appeal on any other substantial question of law not formulated by it, if it is satisfied that the case involves such question.

The High Court shall decide the question of law so formulated and deliver such judgment thereon containing the grounds on which such decision is founded and may award such cost as it deems fit.

The High Court may determine any issue which has not been determined by the Appellate Tribunal or has been wrongly determined by the Appellate Tribunal on such substantial question of law.

Where the High Court delivers a judgement in an appeal filed before it under Section 260A, effect shall be given to the order passed on the appeal by the Assessing Officer on the basis of a certified copy of judgement [Section 260(1A)].

Section 260B provides that an appeal filed under Section 260A shall be heard by a bench of not less than two judges of the High Court and shall be decided in accordance with the opinion such Judges or the majority, if any. Where, however, there is no such majority, the part of law upon which they differ shall be referred to one or more of the Judges of the High Court and shall be decided according to the opinion of the majority of the Judges who have heard the case including those who first heard it.

The High Court also has power to stay a proceeding for recovery of demand arising out of the assessment order pending disposal of appeal.

4.7 APPEAL TO THE SUPREME COURT (SECTION 261)

The aggrieved party is entitled to appeal to the Supreme Court against the judgment delivered by the High Court on the reference application made to it by the Tribunal (under Section 256) against an order made under Section 254 before the 1st day of October, 1998 or an appeal made to High Court in respect of an order passed under Section 254 on or after that date provided the High Court certifies the case to be fit for appeal to the Supreme Court. The right of appeal is, therefore, conditional and may be availed of only if the High Court gives a certificate of such fitness.

The High Court could certify the case as a fit one for appeal and grant leave to the Supreme Court if a substantial question of law is involved or if the question is likely to come up in successive year or if the question is otherwise of great public or private importance.

An application of fitness for appeal to the Supreme Court has to be made within 60 days from the date of High Court's judgment (under Article 132 of the Schedule to the Limitation Act, 1963). The time required for taking a certified copy of the High Court's judgment is to be excluded in computing such period of limitation.

If the High Court refuses to certify a case to be fit for appeal to the Supreme Court, an application may be made to the Supreme Court (under Article 136 of the Constitution) for special leave to appeal against the decision of the High Court.

The provisions of the Code of Civil Procedure, 1908 relating to the appeal to the Supreme Court are applicable in the case of appeals under Section 261 in the same manner as they are applicable in the case of appeals from decrees of a High Court [Section 262(1)].

Where the judgment of the High Court is changed or reversed in the appeal, effect is given to the order of the Supreme Court [Section 262(3)]. The law declared by the Supreme Court is binding on all courts within the territory of India under Article 141 of the Constitution.

On the receipt of a copy of judgment, the Appellate Tribunal has to pass such orders as are necessary to dispose of the case conformably to such judgment.

To award the cost of an appeal is at the discretion the Supreme Court [Section 262(2)]. It would be open to the Court not to award costs even to the party

which has succeeded in the appeal before it. If the Supreme Court awards costs to a party and the party has not complied with the order, a petition may be made to the appropriate High Court for execution of the order of the Supreme Court (Section 266). The High Court may transmit the order for execution to any court subordinate to it (Section 266).

Section 257 enables the Appellate Tribunal to make a direct reference to the Supreme Court if the Tribunal is of the opinion that, on account of a conflict in the decision of High Court in respect of any particular question of law, it is expedient that a reference should be made directly to the highest court.

4.8 ALTERNATE DISPUTE RESOLUTION MECHANISM

With a view to provide speedy disposal in the subject matters of transfer pricing audit and the taxation of foreign company, an alternative dispute resolution mechanism has been provided by inserting section 144C. In this mechanism, the assessing officer, before passing the final assessment order, will serve a draft order on the 'eligible assessee' and the assessee will have an option to accept the draft order or to file his objections on the draft order to Dispute Resolution Panel (DRP). DRP will be collegium of three commissioners of income tax constituted by the Board for this purpose. The DRP shall, in case objections are received from the assessee, issue such directions, as it thinks fit, for the guidance of the Assessing Officer to enable him to complete the assessment. Every direction issued by the DRP shall be binding on the Assessing Officer.

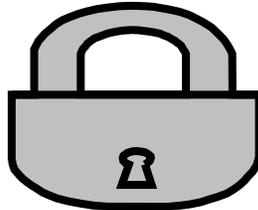
LESSON ROUND UP



- The objectives of tax management are to ensure compliance with tax laws at the specified time and in the specified manner as also to ensure that the tax cost is minimized.
- The return of income has to be signed by the Managing Director in the case of the company and in his absence by one of the Directors.
- The right to appeal must be given by express enactment in the Act. Therefore, in case there is no provision in the Act for filing an appeal regarding a particular matter, no appeal shall lie. The right to appeal arises where the taxpayer is aggrieved by the order passed by the income-tax authority.
- The assessee may prefer an appeal against the orders of the Assessing Officer to the Commissioner (Appeals), in accordance with the relevant provisions under Section 246 and appeal against the order of the Commissioner (Appeals) can be preferred by the Assessee or the Commissioner of Income Tax and such appeal lies with the Appellate Tribunal.
- The Central Government shall constitute an Appellate Tribunal consisting of as many judicial and accountant members as it thinks fit to exercise the powers and discharge the functions conferred on the Appellate Tribunal by this Act.

- Section 260A provides that an appeal shall lie to the High Court from every order passed in appeal by the Appellate Tribunal if the High Court is satisfied that the case involves a substantial question of law.
- The aggrieved party is entitled to appeal to the Supreme Court against the judgment delivered by the High Court.

SELF-TEST QUESTIONS



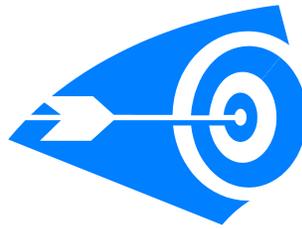
1. Compliance with legal formalities is less costly than the payment of penalty or interest due on taxes. Explain the statement briefing the defaults and penalties under the Income-tax Act.
2. Explain the provisions with respect to appeals and revisions with reference to tax planning.
3. Explain the provisions relating to revision of assessment order prejudicial to the interest of assessee.
4. What are the various grounds of appeals available before different types of authorities to the assessee?
5. Under what circumstances the assessment order can be revised on the basis of applications of the assessee? Under what circumstances the revision cannot be made ?
6. Under what circumstances can an assessee appeal to the Appellate Tribunal? What documents are to be attached in mailing an appeal to the Tribunal?
7. When can an aggrieved party appeal to the Supreme Court against the judgment delivered by the High Court?

PART B – INDIRECT TAXATION—LAW AND PRACTICE

STUDY V

INTRODUCTION

LEARNING OBJECTIVES



The objective of the study lesson is to enable the students to understand:

- Pervasive nature of indirect taxation
- Constitutional Provisions
- Levy and collection of duties:
 - (a) Central Excise
 - (b) Customs
 - (c) Central Sales Tax
 - (d) Service Tax
 - (e) VAT

5.1 INTRODUCTION

Taxes are conventionally divided into direct tax and indirect tax. Indirect tax includes Customs, Central Excise, Service Tax, Central Sales Tax and VAT. In case of indirect taxes the tax burden is shifted from one person to another. As indirect taxes are usually or generally imposed on an *ad valorem* basis, the major portion of revenues from these taxes increases automatically with rise in commodity prices. Indirect taxation is also known as commodity taxation as the excise levy is made in respect of commodities manufactured in any part of India. As the name suggests the end consumer is not directly associated with burden as the manufacturer (otherwise usually associated). As per records, indirect tax contributes almost 70% of total tax revenue to the Government. Indirect taxes are easier to collect and they do not discriminate between rich and poor. There is least chance of tax evasion in case of indirect taxes. It is based on principle of equity.

5.2 CONSTITUTIONAL PROVISIONS

Article 246 of the Constitution of India indicates bifurcation of powers to make laws between Union Government and State Governments. Article 246(1) of

Constitution states that Parliament has exclusive powers to make laws with respect of any of matters enumerated in List I in the Seventh Schedule to Constitution (Called Union List). As per Article 246(3) State Government has exclusive powers to make laws for State with respect to any matter enumerated in List II of Seventh Schedule to Constitution (Called State List). As per Article 246(2) Parliament as well as the State Legislature has power to make laws with respect to any matters enumerated in the List III of the Seventh Schedule to the Constitution (called concurrent list).

Items in the Union List (List I) in respect of which Parliament has exclusive powers to levy taxes:

Entry No.82 – Tax on income other than agricultural income.

Entry No.83 – Duties of custom on goods imported into or exported from India.

Entry No.84 – Duties of excise on tobacco and other goods manufactured or produced in India except alcoholic liquors for human consumption, opium, narcotic drugs, but including medicinal and toilet preparations containing alcoholic liquor, opium or narcotics.

Entry No. 85 – Corporation Tax.

Entry No.92A – Taxes on the sale or purchase of goods other than newspapers, where such sale or purchase takes place in the course of interstate trade or commerce.

Entry No.92B – Taxes on consignment of goods where such consignment takes place during interstate trade or commerce.

Entry No.92C – Tax on services (Not yet notified).

Entry No.97 – Any other matter not included in List II, List III and any tax not mentioned in List II or List III.

5.3 CENTRAL EXCISE

The Central Excise Act, 1944 is the basic Act provided for charging of duty, valuation, powers of the authorities, penal provisions etc. It has been amended from time to time in the Union Budgets. Section 37 of the Central Excise Act (CEA) grants power to the Government of India to frame Rules for prescribing procedures, forms etc. These Rules are amended from time to time. There is Central Excise (determination of price of excisable goods) Rules 2000 which deals with basic provisions for determining value as per Section 4 of the Central Excise Act. However, in certain cases the value cannot be fixed purely on the basis of Section 4 for which rules have been described under section 4(1)(b) of the Central Excise Act, 1944. Under sections 5A and 11C of Central Excise Act, the Central Government has been granted power to issue notifications for granting exemptions from excise duty. The classification of items under excise law is stated under Central Excise Tariff Act, 1985 (CETA). The Tariff Act contains 96 chapters and each item comprised in this chapter are codified. An additional duty is levied on goods of special importance (like sugar, cigarettes) under additional duty of Excise Act, 1957. The textile articles have been granted exemption with effect from 9.7.2004. Once duty liability is fixed, the

duty can be collected from a person at the time and place found administratively most convenient for collection. According to Guideline Notes of ICAI on accounting treatment for excise duty in the monthly *chartered accountant* (July 2000), excise duty has been considered as a manufacturing expense and should be considered an element of cost for inventory valuation like manufacturing expenses. Education cess is applicable for excisable duty. As per section 3(3) of AED (GSI) Act, 1957 provisions of Central Excise including those related to the refund, exemptions, offences and penalties in relation to levy and collection of duties shall be applicable to AED (GSI) also. At present AED (GSI) is exempt from duty.

5.4 CUSTOMS LAW

The Customs Act 1962 has consolidated the provisions relating to the Sea Customs Act, Land Customs Act and Air Customs Act which existed separately. During 1965 and 1971 import tariff rates were rationalized. In 1975 the Customs Tariff Act, 1975 was passed replacing the Indian Tariff Act, 1934 which originally provided for the levy of import and export duties. The rates of which the customs duties shall be levied under this Act are specified in the First and Second Schedules. The Customs Tariff Act, 1975, was mainly based on Brussels nomenclature. The changes in the Customs Tariff are announced at the time of Budget of the Country. In 1985, the Customs Co-operation Council developed a new system of nomenclature known as the Harmonised Commodity Description and Coding System. India too adopted this system by making an amendment to the Customs Tariff Act, 1975, by substituting a new Customs Tariff Schedule.

The main objective of the Customs Act is to safeguard the domestic trade, raise revenue resources for economic development of the country, checking smuggling activities and prevent any unauthorized dumping of foreign goods.

The main rules and regulations under the Customs Act are as follows:

- (i) The Customs Valuation Rules, 2007.*
- (ii) Duty Drawback Rules, 1995.*
- (iii) Re-export of imported goods Drawback of Custom Rules, 1995.*
- (iv) The Baggage Rules, 1998.*
- (v) Project Import Regulations, 1986.*
- (vi) Provisional Assessment Regulations, 1963*
- (vii) Import Manifest (Vessels) Regulation, 1976*
- (viii) Bill of Entry Form Regulations, 1976*
- (ix) Customs House Agents Regulations*
- (x) Bill of Entry (Electronic Declaration) Regulations, 1995.*

Customs Act, 1962 was passed by the Parliament on 13th December, 1962. The Act came into force on February 1, 1963. The Act extends to the whole of India. It is a simple, crisp and lucid piece of enactment. It is primarily treated as a Revenue Act.

Its main object is to collect duties on exports and taxes on imports under the fiscal laws and tariffs. The Customs Act consists of 17 Chapters and 161 Sections.

5.5 CENTRAL SALES TAX ACT

According to Entry 54 appearing in List II of the 7th Schedule read with Article 246(3), the states has been empowered to imposed taxes on sale and purchase of goods other than newspapers subject to the provisions of Entry 92(A) of the union list.

Central Sales Tax Act, 1956 describing levy of tax on inter-state sale and purchase of goods came into force from July 1st, 1956. Consequently, article 286 of the constitution was amended. By the amendment of articles 269(3) of the constitution, parliament is empowered to formulate the principals for determining when sale or purchase of goods takes place in the course of inter-state trade and commerce or outside state or in the course of import into or export from India. The main purpose of Central Sales Tax is to formulate on which inter-state trade or commerce will take place. It also used for levy, collection and distribution of taxes on sales of goods in the course of inter-state trade or commerce. Moreover, the Act also contains provisions relating to restrictions and conditions associated with the inter-state trade or commerce.

The main provisions of the Act deal with the following items:

- (i) Inter-state sales (Section 3);*
- (ii) Sale or purchase of goods taking place outside a State (Section 4);*
- (iii) Sale or purchase in the course of export and import (Section 5);*
- (iv) Liability and charge to sales tax (Section 6);*
- (v) Registration of dealers (Section 7);*
- (vi) Determination of taxable turnover (Section 8);*
- (vii) Levy and collection of tax (Section 9);*
- (viii) Offences (Section 10 to 12);*
- (ix) Declared goods (Section 14 and 15).*

The constitution 46th amendment in 1982 has amended articles 269, 286 and 366 and inserted a new Entry 92B in the Union List of the Seventh Schedule. The Act deals with two types of goods namely, declared goods and other goods. The rate of tax was initially stated at 4% and 10% with respect to transactions with registered dealers and non-registered dealers respectively. With the promulgation of VAT by majority of Indian States, it has been decided to phase out Central Sales Tax.

5.6 SERVICE TAX

As the economy grows and develops, the contribution of the services sector becomes more substantial. Hence, tax on services becomes substantial revenue for the Government. Although Service tax is a concept of the modern era where developed economies as well as developing economies find over 70% of their gross economic output coming from the service sector. Service tax was there in vogue even in the Mauryan period in India. Ms. Romila Thaper in her "Asoka and the

Decline of the Mauryas”, at page 72 (London 196, paperback edition, 1997, by Oxford) points out that services of weapon and implement makers were required to be provided to the state for a certain number of days in a year. This was a form of service tax in that period. But in the modern context, because of the increasing contribution of the service sector to the GDP of an economy, the importance of service tax is growing. As under the WTO agreements governments are required to reduce customs tariffs, governments are considering increase in service taxes revenues as a compensatory revenue generation mechanism. In terms of economics, tax on services is an indirect tax. This is because the burden of service tax can be passed on to the customer i.e., the recipient of the service. The service provider may also bear the burden of the tax by not charging the service tax separately in the invoice.

The Tax Reforms Committee headed by Dr. Raja J Chelliah recognized the revenue potential of the service sector and recommended imposition of service tax on selected services. Consequently the service tax was imposed at a uniform rate of 5% in the Union Budget for 1994-95 on 3 services.

Finance Act, 2012 has made remarkable changes in service tax legislation whereby the concept of Positive list of Taxable services has been replaced with a negative list. A negative list of services implies two things; firstly, a list of services which are not be subject to service tax; secondly, other than services mentioned in the negative list or exempted list, all other services became taxable which fall within the definition of services. This is in contrast to the present method of taxation that has detailed description for each taxable service and all other unspecified services are not liable to tax.

5.6.1 Constitutional Validity

As per article 246 of the constitution of India law can be enacted by parliament or the state legislature, if such power is given by the constitution of India.

Article 265 of the Constitution lays down that no tax shall be levied or collected except by the authority of law. Schedule VII divides this subjects into three categories—

- (a) Union list (only Central Government has power of legislation)*
- (b) State list (only State Government has power of legislation)*
- (c) Concurrent list (both Central and State Government can pass legislation).*

Entry 97 of the union list is the residuary entry and empowers the central government to levy tax on any matter not enumerated in state list or the concurrent list.

In 1994, the service tax was levied by the central government under the power granted by the entry 97 of the union list.

Thereafter, in 2003 the government has passed the constitution (88th Amendment Act, 2003) which provides for the levy of service tax by the centre through the insertion of article 268A to the constitution. In addition to article 268A, entry 92C has been inserted in the union list to make the enactment relating to service tax a subject matter of union list.

Students may note that entry No.92C has not yet been made effective by the parliament and service tax is still governed by the entry 97 of the union list.

Certain provisions of the Central Excise Act, 1944 also apply to Service Tax. The various limbs of the Service Tax Law are:

1. The provisions of the Finance Act, 1994 as amended by successive Finance Acts;
2. Service Tax Rules, 1994, as amended from time to time;
3. The CENVAT Credit Rules, 2004 in to which the Service Tax Credit Rules, 2002 have been merged;
4. Statutory Notifications on service tax issued by the Government;
5. Circulars on service tax issued by the CBEC;
6. Trade Notices issued by jurisdictional Commissionerates of Central Excise or Service Tax on service tax matters.

5.6.2 Scope

To begin with only telephone, stock broker and general insurance services were brought into the tax net. The Finance Act, 1996 enlarged the scope of the service tax to cover additionally, advertising, pager and courier services. The subsequent Finance Act gradually went on increasing the number of taxable services.

Service tax is levied on taxable services. The levy of service tax dealt in section 66 (charging section), which provides that service tax is levied at a specific rate on the value of taxable services referred to in section 65(105) of the Act. However, with the insertion of a proviso in section 66, the provisions of this section will cease to apply with effect from July 1, 2012.

Therefore, with effect from 1st July 2012, a new charging Section 66B has been inserted by the Finance Act, 2012. Section 66B provides that there shall be levied a service tax at the rate of twelve per cent on the value of all services, except the services specified in the negative list, provided or agreed to be provided in the taxable territory by a person to another and collected in the prescribed manner.

Steps to determine the Taxability of service under Negative List Regime

1. Check whether the activity falls within the definition of service and declared services.
2. if it is service then, check whether the service provided is excluded either by the negative list or is otherwise exempted.
3. If it is so covered, then check the applicability of Place of Provision of Services Rules.

5.6.3 Computation of Tax

Rate of Service Tax

The rate of service tax is itself mentioned in the charging section. As per the new charging section 66B service tax is leviable @12% on the value of all services. Further, education cess of 2% plus secondary and higher education cess of 1% is levied.

Computation of Tax

If a person renders a taxable service of the value of ₹ 500, the service tax @12% will be ₹ 60. The education cess and Secondary & Higher education cess @3% on ₹ 60 will be ₹ 1.80. The total tax will be ₹ 61.80.

Value of Taxable Services

Where the gross amount charged by a service provider is inclusive of service tax payable, the value of taxable service shall be such amount as with the addition of tax payable, is equal to the gross amount charged. Service tax is levied on services provided within the territory of India including territorial waters of India extending upto 12 nautical miles (under International Sea Act). Hence services provided beyond the territorial waters of India are not liable to service tax as the provisions of the service tax have not been extended to such areas so far.

5.7 VALUE ADDED TAX (VAT)

Introduction

The Value Added Tax (VAT) in India is a state level multi-point tax on value addition which is collected at different stages of sale with a provision for set-off for tax paid at the previous stage i.e., tax paid on inputs. It is to be levied as a proportion of the value added (i.e. sales minus purchase) which is equivalent to wages plus interest, other costs and profits. It is a tax on the value added and can be aptly defined as one of the ideal forms of consumption taxation since the value added by a firm represents the difference between its receipts and cost of purchased inputs. Value Added Tax is commonly referred to as a method of taxation whereby the tax is levied on the value added at each stage of the production/distribution chain. As against the existing regime under which goods are charged to tax at Single point, or multi-point on the value of the goods, without any credit being given for taxes paid at the preceding stages. VAT intends to tax only the value added at each stage and not the entire invoice value of the product. By ensuring that only the incremental value is taxed, VAT aims at eliminating the cascading effect of taxes on commodities, and thereby reduces the eventual cost to the consumer.

It is one of the most radical reforms, albeit only in the sphere of State level taxes on sale, those have been initiated for the Indian economy after years of political and economic debate aiming at replacing complicated tax structure to do away with the fraudulent practices.

With the objective to introduce State-Level VAT in India in the Year 1992, the Government of India constituted a Tax Reform Committee headed by Dr. Raja J. Chelliah. In 1993, the Committee recommended the introduction of VAT in place of existing tax system. Thereafter, the Government appointed NIPFP (National Institute of Public Finance and Policy), New Delhi, as the Nodal Agency to work out the modalities of VAT.

The first preliminary discussion on State-Level VAT took place in a meeting of Chief Ministers convened by Dr. Manmohan Singh, the then Union Finance Minister in 1995. In this meeting, the basic issues on VAT were discussed in general terms and this was followed up by periodic interactions of State Finance Ministers.

For implementing the above decisions, an Empowered Committee of State Finance

Ministers was set-up. Thereafter, this Empowered Committee met frequently and got full support from the State Finance Ministers, the Finance Secretaries and the Commissioners of Commercial Taxes of the State Governments as well as Senior Officials of the Revenue Department of the Ministry of Finance, Government of India. Through repeated discussions and collective efforts of all, it was possible to achieve remarkable success within a period of about one and half years. After reaching this stage, steps were initiated for the systematic preparation for the introduction of State-Level VAT.

Along with these measures ensuring convergence on the basis issues on VAT, steps were taken for necessary training, computerization and interaction with trade and industry, particularly at the State level. This interaction with trade and industry was specially emphasized. The conference of State Chief Ministers presided over by Shri Atal Behari Vajpayee, the then Prime Minister, held on October 18, 2002 at which Shri Jaswant Singh, the then Finance Minister was also present, confirmed the final decision that all the States and the Union Territories would introduce VAT from April 1, 2003.

A White Paper on State-Level Value Added Tax (VAT) by The Empowered Committee of State Finance Ministers (Constituted by the Ministry of Finance, Government of India on the basis of Resolution Adopted in the Conference of the Chief Ministers on November, 16, 1999, New Delhi, January 17, 2005. The Empowered Committee in the White Paper has justified the introduction of VAT in the following words:

“In the existing sales tax structure, there are problems of double taxation of commodities and multiplicity of taxes, resulting in a cascading tax burden. For instance, in the existing structure, before a commodity is produced, inputs are first taxed, and then after the commodity is produced with input tax load, output is taxed again. This causes an unfair double taxation with cascading effects. In the VAT, a set-off is given for input tax as well as tax paid on previous purchases. In the prevailing sales tax structure, there is in several states also a multiplicity of taxes, such as turnover tax, surcharge on sales tax, additional surcharge, etc. With introduction of VAT, these other taxes will be abolished. In addition, Central Sales Tax is also going to be phased out. As a result, overall tax burden will be rationalized, and prices in general will also fall. Moreover, VAT will replace the existing system of inspection by a system of built-in self-assessment by the dealers and auditing. The tax structure will become simple and more transparent. That will improve tax compliance and also augment revenue growth..... The VAT will therefore help common people, traders, industrialists and also the Government. It is indeed a move towards more efficiency, equal competition and fairness in the taxation system”.

The first preliminary discussion on State-level VAT took place in a meeting of Chief Ministers convened by Dr. Manmohan Singh, the Union Finance Minister in 1995. In this meeting, the basic issues on VAT were discussed in general terms and this was followed up by periodic interactions of States Finance Ministers. Thereafter, in a significant meeting of all Chief Ministers, convened on November 16, 1999 by Shri Yashwant Sinha, the then Union Finance Minister, three important decisions were taken. First, before the introduction of State-level VAT, the unhealthy sales tax rate “war” among the States would have to end and sales tax rates would need to be harmonized by implementing uniform floor rates of sales tax for different categories

of commodities with effect from January 1, 2000. Second, in the interest again of harmonization of incidence of sales tax, the sales-tax-related industrial incentive schemes would also have to be discontinued with effect from January 1, 2000. Third, on the basis of achievement of the first two objectives steps would be taken by the states for introduction of State-level VAT after adequate preparation. For implementing these decisions, an Empowered Committee of State Finance Ministers was set-up.

Thereafter, this Empowered Committee has met regularly, attended by the state Finance Ministers, and also by the Finance Secretaries and the Commissioners of Commercial Taxes of the State Governments as well as senior officials of the Revenue Department of the Ministry of Finance, Government of India. Through repeated discussions and collective efforts in the Empowered Committee, it was possible within a period of about a year and a half to achieve nearly 98 per cent success in the first two objectives on harmonization of sales tax structure through implementation of uniform floor rates of sales tax and discontinuation of sales-tax related incentive schemes. As a part of regular monitoring, whenever any deviation is reported from the uniform floor rates of sales tax, or from decision on incentives, the Empowered Committee takes up the matter with the concerned state and also the Government of India for necessary rectification.

The Committee of Finance Minister (in 1995 and 1998) has put forward recommendations to replace sales tax by Value Added Tax (VAT). Further the conference of Chief Minister and the Finance Minister has proposed introduction of VAT by April 1, 2002 with uniform floor rates. The Empowered Committee of State Finance Ministers on February 8, 2003 again endorsed the suggestion that all the State legislations on VAT should have a certain minimum set of common features. Most of the States came out with their respective draft legislations. Shri Jaswant Singh the then Union Finance Minister, also announced the introduction of VAT from 1st April, 2003 in his 2003-2004 budget speech made on February 28, 2003. Owing to some unavoidable circumstances, VAT could not be implemented w.e.f. April 1, 2003 and also on the revised date June 1, 2003, despite all obstacles, Haryana was the first State to implement VAT w.e.f. April 1, 2003. In rest of the States VAT Laws were at draft stage.

The Empowered Committee of the State Finance Ministers constituted by the Ministry of Finance, Government of India, on the basis of the resolution adopted in the conference of the Chief Ministers on November 16, 1999 under the Chairmanship of Dr. Asim Dasgupta came out with a White Paper on State-Level VAT, which was released on January 17, 2005 by Shri P. Chidambaram, The Finance Minister, Government of India. On this occasion the Finance Minister remarked:

“This is the first document which has been collectively prepared and put out to the people of the country by the Finance Ministers of all States.... We have formed the rainbow coalition to undertake one of the biggest tax reforms.”

This Paper consists of three parts. In Part I, justification of VAT and the background has been mentioned. In Part II, main Design of VAT as evolved on the basis of consensus among the States through repeated discussions in the Empowered Committee has been elaborated. In Part III, other related issues for effective implementation of VAT have been discussed.

The White Paper specified that registration under the VAT Act shall not be

compulsory for the small dealers with gross annual turnover not exceeding ₹5 lakh. However, the Empowered Committee of State Finance Ministers has subsequently allowed the States to increase the threshold limit for the small dealers to ₹10 lakh, but the concerned State shall have to bear the revenue loss, on account of increase in the limit beyond ₹5 lakh. The VAT Acts are designed so that high value taxpayers should not be spared and on the contrary small dealers should be hassle free from compliance procedures.

The objective of all such composition schemes is not to burden small dealers by the provisions of record keeping. Therefore, such schemes will generally contain the following features:

- (i) small amount of tax shall be payable;*
- (ii) there shall be no requirement to calculate taxable turnover;*
- (iii) a simple return form to cover longer return form shall be sufficient.*

All sales or purchases of goods made within the State except the exempted goods would be subjected to VAT as a consumption tax.

In his speech introducing Union Budget 2005-06, the Hon'ble Finance Minister said, "In a remarkable display of the spirit of cooperative federalism, the States are poised to undertake the most important tax reform ever attempted in this country. All States have agreed to introduce the Value Added Tax (VAT) with effect from April 1, 2005. VAT is a modern, simple and transparent tax system that will replace the existing sales tax and eliminate the cascading effect of sales tax.

In the medium to long term, it is my goal that the entire production/distribution chain should be covered by a national VAT, or even better, a goods and services tax, encompassing both the Centre and the States.

The Empowered Committee of the State Finance Ministers, with the solid support of the Chief Ministers, has laboured through the last seven years to arrive at a framework acceptable to all States. The Central Government has promised its full support and has also agreed to compensate the States, according to an agreed formula, in the event of any revenue loss. I take this opportunity to pay tribute to the Empowered Committee, and wish the States success on the introduction and implementation of VAT".

5.7.1 Methods of Computation

VAT can be computed by using any of the three methods detailed below:

- 1. The Subtraction method:** Under this method the tax rate is applied to the difference between the value of output and the cost of input;
- 2. The Addition method:** Under this method value added is computed by adding all the payments that are payable to the factors of production (viz., wages, salaries, interest payments, profit etc.);
- 3. Tax Credit method:** Under this method, it entails set-off of the tax paid on inputs from tax collected on sales. Indian States opted for tax credit method, which is similar to CENVAT.

5.7.2 Procedure

The VAT is based on the value addition to the goods and the related VAT liability of the dealer is calculated by deducting input tax credit from tax collected on sales during the payment period. This input tax credit is given for both manufacturers and traders for purchase of input/supplies meant for both sales within the State as well as to the other States irrespective of their date of utilization or sale. If the tax credit exceeds the tax payable on sales in a month, the excess credit will be carried over to the end of the next financial year. If there is any excess unadjusted input tax credit at the end of the second year then the same will be eligible for refund. For all exports made out of the country, tax paid within the State will be refunded in full. Tax paid on inputs procured from other States through inter-State sale and stock transfer shall not be eligible for credit.

The existing Sales Tax Acts in all states will give place to the State VAT Act. Accordingly the rules, schedules and Forms under the erstwhile Acts will be abolished. However, Central Sales Tax will continue to govern inter-State Sales and Exports.

5.7.3 Rates of Tax

As contrasted to the multiplicity of rates under the existing regime, VAT will have 4 broad rates-

- 0% (Exempted) for unprocessed agricultural goods, and goods of social importance),
- 1% for precious and semiprecious metals,
- 4% for inputs used for manufacturing and on declared goods, capital goods and other essential items,
- 20% for demerit/luxury goods and
- the rest of the commodities will be taxed at a Revenue Neutral Rate of 12.5%.

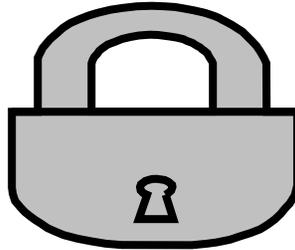
LESSON ROUND UP



This chapter includes:

- Introducing various components of Indirect Taxation and Constitutional Provisions
- Levy and collection of duties:
 - (a) Central Excise
 - (b) Customs
 - (c) Central Sales Tax
 - (d) Service Tax
 - (e) VAT

SELF-TEST QUESTIONS



1. Discuss briefly the constitutional provisions regarding Indirect taxes in India
2. Write in short on the procedural aspects in the imposition of excise duty and customs duty in India.
3. What is VAT? How is it computed?
4. Explain briefly how service tax is computed.
5. What is cascading effect of taxes on commodities?

STUDY VI
CENTRAL EXCISE LAWS
LEARNING OBJECTIVES



The objective of the study lesson is to enable the students to understand:

- Basis of Levy of Excise Duty
- Basis of Chargeability of Excise Duty
- Concept of “Goods”
- Concept of “Excisable Goods”
- Production, Manufacture and Process distinguished
- Concept of “Manufacturer”
- Classification of Goods
- Valuation of Goods Under Central Excise Law
 - Methods of Valuation
 - Valuation Based on MRP
 - Scope and objects
 - Valuation under Section 4
 - Transaction Value
- Procedure for fixation of value under Section 4
- The Central Excise Valuation (Determination of Price of Excisable Goods) Rules, 2000
- The Central Excise (Determination of Retail Sale Price of Excisable Goods) Rules, 2008
- Payment of Excise Duties
- Clearance and Removal Procedures
 - Self Assessment Method
 - Removal of goods on invoice
 - Compounded Levy Scheme
- Remission of Duty (Rule 21)
- Filing of return and E-Filing of return
- Large Tax Payer Units
- Excise Duty — Exemptions
- Recovery of sums due to Government (Section 11)
- Recovery of duties not levied or not paid or short levied or short paid or erroneously refunded (Section 11A)
- Interest on delayed payment of duty (Section 11AA)
- Claim for refund of duty and interest, if any paid on such duty (Section 11B)
- Doctrine of Unjust Enrichment
- Payment of Interest on delayed refund (Section 11BB)
- Power not to recover duty of excise not levied or short levied as a general practice (Section 11C)
- Excise Audit - 2000
- Deposit of Central Excise Duty During Strikes in Nominated Banks

- Appellate Procedures and Search, Seizure and Investigation
 - The Appellate Scheme
 - The Customs, Excise, Service Tax Appellate Tribunal (CESTAT)
 - Appeals before Commissioner (Appeals) (Section 35)
 - Further remedies after decision by CESTAT
 - Powers of Committee of Chief Commissioners of Central Excise or Commissioner of Central Excise to pass certain orders on its own (Section 35E)
- Deposit Pending appeal of duty demanded or penalty levied (Section 35F)
- Interest on delayed refund of amount deposited under the proviso to Section 35F (Section 35FF)
- Revisionary Role of The Central Government
- Settlement Commission
 - Powers and Duties of Officers
 - Power of Adjudication
 - Procedure to be followed in cases where duty is paid under protest
 - Special Audit in certain cases (Section 14A)
 - Special Audit in cases where credit of duty availed or utilized is not within normal limits etc. (Section 14AA)
- CENVAT Credit Rules 2004
- Small Scale Industries
- Conclusion
- Annexures

6.1 BASIS OF LEVY OF EXCISE DUTIES

The power to levy and collect excise duties has been conferred on the Union Government by virtue of Article 246 of the Constitution of India.

Entry 84 of the Union List empowers the Government to levy duty of Excise on Tobacco and other goods manufactured or produced in India excluding alcoholic liquors for human consumption opium Indian hemp and other narcotic drugs and narcotics but including medicinal and toilet preparations containing alcohol or opium, Indian hemp or other narcotic drugs.

It means that only the goods, which are produced or manufactured in India can become liable to excise duties.

Thus, the statutory authority to levy duty of excise has been conferred by the Constitution on the Union Government.

6.2 BASIS OF CHARGEABILITY OF EXCISE DUTY

Section 3 of Central Excise Act, 1944 empowers the Central Government to levy duty of excise on excisable goods produced or manufactured in India. Section 3 is a charging section.

As per Section 3(1), there shall be levied and collected in such manner as may be prescribed:

- (a) a duty of excise to be called the Central Value Added Tax (CENVAT) on all excisable goods (excluding goods produced or manufactured in special economic zones) which are produced or manufactured in India as, and at the rates, set forth in the First Schedule to the Central Excise Tariff Act, 1985 (5 of 1986);
- (b) a special duty of excise, in addition to the duty of excise specified in clause (a) above, on excisable goods specified in the Second Schedule to the Central

Excise Tariff Act, 1985 (5 of 1986) which are produced or manufactured in India, as, and at the rates, set forth in the said Second Schedule.

Provided that the duties of excise which shall be levied and collected on any excisable goods (excluding goods produced or manufactured in special economic zones) which are produced or manufactured—

- (i) in a free trade zone and brought to any other place in India (omitted by Finance Act,2007 w.e.f. 11.05.2007)
- (ii) by a hundred per cent export oriented undertaking and brought to any other place in India,

shall be an amount equal to the aggregate of the duties of customs which would be leviable under the Customs Act, 1962 (52 of 1962) or any other law for the time being in force, on like goods produced or manufactured outside India if imported into India, and where the said duties of customs are chargeable by reference to their value; the value of such excisable goods shall, notwithstanding anything contained in any other provision of this Act, be determined in accordance with the provisions of the Customs Act, 1962 (52 of 1962) and the Customs Tariff Act, 1975 (51 of 1975).

Explanation 1.— Where in respect of any such like goods, any duty of customs leviable for the time being in force is leviable at different rates, then such duty shall, for the purposes of this proviso, be deemed to be leviable at the highest of those rates.

Explanation 2.— In this proviso—

- (i) **“free trade zone”** means a Zone which the Central Government may, by notification in the Official Gazette, specify in this behalf (omitted by Finance Act,2007 w.e.f. 11.05.2007)
- (ii) **“hundred per cent export-oriented undertaking”** means an undertaking which has been approved as a hundred per cent export-oriented undertaking by the Board appointed in this behalf by the Central Government in exercise of the powers conferred by Section 14 of the Industries (Development and Regulation) Act, 1951 (65 of 1951), and the rules made under the Act.
- (iii) **“special economic zone”** means a zone which the Central Government may by notification in the Official Gazette, specify in this behalf.

Sub-section (1A) of Section 3 provides that the provisions of Sub-section (1) shall apply in respect of all excisable goods other than salts which are produced or manufactured in India by, or on behalf of, Government, as they apply in respect of goods which are not produced or manufactured by Government.

As per Sub-section (2) the Central Government may, by notification in the Official Gazette, fix, for the purpose of levying the said duties, tariff values of any articles enumerated, either specifically or under general headings, in the First Schedule and the Second Schedule to the Central Excise Tariff Act, 1985 (5 of 1986) as chargeable with duty *ad valorem* and may alter any tariff values for the time being in force.

Sub-section (3) provides for different tariff values may be fixed—

- (a) for different classes or descriptions of the same excisable goods; or,
- (b) for excisable goods of the same class or description —
 - (i) produced or manufactured by different classes of producers or manufacturers; or
 - (ii) sold to different classes of buyers:

Provided that in fixing different tariff values in respect of excisable goods falling under sub-clause (i) or sub-clause (ii), regard shall be had to the sale prices charged by the different classes of producers or manufacturers or, as the case may be, the normal practice of the wholesale trade in such goods.

Through Section 3, the Union legislature has thus, done the following:

- (a) Created the duty;
- (b) Given a name to the duty;
- (c) Conferred the authority to levy and collect the duty;
- (d) Defined the scope of the duty;
- (e) Provided for specifications of the rates at which the duty shall be charged.

Presently, under Section 3(2), pan masala packs below 10 grams are covered.

Section 3 the charging section have identified four basic condition for taxability of goods. For anything to be liable to excise duties, it must fulfill all the following conditions:

- (a) It must be "goods";*
- (b) It must be "excisable goods";*
- (c) It must be either produced or manufactured*
- (d) Such manufacture or production must be in India.*

Taxable Event

While the duty no doubt is on goods as such, still, goods themselves cannot pay duty. This takes us to the next concept of "taxable event". For every tax, whether direct or indirect, there is a "taxable event". That is the event or situation which gives rise to the liability to the tax in question being created. In regard to import duties, it is the act of import which creates the liability. In as much as excise duties are duties on goods produced/manufactured, the taxable event is production or manufacture. Since, as noted, goods cannot pay duty, the *person* who created the taxable event is the person who must discharge the liability which he has created, which would mean that he should be the person to pay the duty. Since the taxable event is production/manufacture, by implication, the person who is to pay the excise duty is the producer or the manufacturer. Hence, the last of the basic concepts which will determine the duty liability in Central Excise is "manufacturer/ producer".

As for the linguistic dichotomy incorporated in Section 3, the legislature had to mention both manufacture and production since there are a few excisable goods which cover unmanufactured goods as well (e.g. unmanufactured tobacco).

The four basic concepts in Central Excise having thus been identified, we may now examine the scope and meaning of each such concept and the controversies pertaining to it as well. If we analyse the controversies, it will become apparent that most of them owe their origin to the compulsive urge which is natural to every assessee, which is to curtail the tax liability to the utmost, and if possible, to keep away from the liability itself. In this context, the basic concepts have lent themselves substantially to such attempts, since any person who is considered by the department as liable to duty can attempt (and at times successfully too) to prove that he is *not* so liable.

6.2(a) The concept of "Goods"

Excise duty is a duty on goods. The Explanation to the Section 2 (d) of the Central

Excise Act (inserted w.e.f 10.05.2008) has provided a definition of the term “goods” for the purpose of defining “excisable goods”. Accordingly,

“goods” includes any article material or substance which is capable of being bought and sold for a consideration and such goods shall be deemed to be marketable.

Further, the scope of the term “goods” can be derived from various definitions available elsewhere:

- (a) **Article 366(12) of the Indian Constitution** contains an inclusive definition which says that “goods” includes all materials commodities and articles. Being an inclusive definition, this does not help much in pin-pointing the meaning of term as such.
- (b) **Section 2(22) of the Customs Act, 1962** defines “goods” to include vessels, aircraft and vehicles; stores; baggage; currency and negotiable instruments and “any other kind of moveable property”. This definition framed specifically for Customs purposes may not be of much utility as determining the scope of “goods” indigenously manufactured, for purposes of excise taxation.
- (c) **Section 2(7) of the Sale of Goods Act, 1930** defines “goods” as to mean “every kind of movable property other than actionable claims and money; and includes stock and shares, growing crops, grass and things attached to or forming part of the land which are agreed to be severed before sale or under the contract of sale”. While the second part of this definition is of an inclusive nature, the first part is quite specific. According to this definition, every kind of movable property other than actionable claims constitute ‘goods’.
- (d) **The Supreme Court in the case of Union of India v. Delhi Cloth and General Mills (Civil Appeals 168–170 of 1960)** while examining this issue had occasion to go into certain dictionary meanings. They referred to a book “Words and Phrases” Permanent Edition Volume 18 which in turn quoted a judgement of the New York Court. The learned judge had observed that the word ‘goods’ is defined in Bailey’s larger Dictionary of 1732 simply as “merchandise” (the spelling presumably was one which prevailed in 1732). He also cited the great lexicographer Dr. Samuel Johnson who defined ‘goods’ as “movables in a house; personal or immovable estate; wares; freight, merchandise”.
- (e) Coming to more recent times, *Websterdehnes* the word thus: “Goods, Noun, Plural: (1) Moveables, household furniture; (2) personal or moveable estate, as horses, cattles, utensils, etc. (3) wares, merchandise, commodities bought and sold by merchants and traders”.
- (f) Deriving considerable inspiration from the Webster’s definition, **the Supreme Court in the DCM case** stated that for excise purposes, anything will become goods **only if it is either sold or is capable of being sold**. The stress they placed on saleability as the deciding criterion appears to be on the ground that since excise is a duty on goods at the stage of manufacture, and manufacture is mostly for purposes of sale, it is saleability which is the crucial criterion.

In any event, the principle enunciated by the Supreme Court in the DCM case had stood the test of time, and we can well say that though there is no statutory definition of the word 'goods' in Central Excise law, the correct scope of the word has crystallised by now and **it is those movable things that are either sold or are capable of being sold, constitute 'goods' for purposes of levy and collection of excise duties.**

Thus, movability and marketability are the two constituents of goods which require close study.

MOVABILITY

Movability is an inherent and inseparable feature of goods whereas marketability is an integral part of excisable goods. Because excise levy is on the event of manufacture, it presupposes that only movable goods are manufactured; roads, dams, buildings etc. are not manufactured. So, anything that comes into existence as immovable cannot be subjected to levy under excise as immovables cannot be manufactured; they can only be constructed, built and so on. Hence, the entire discussion on excisable goods revolves round the two concepts movability and marketability. Since excisability can be attached to manufactured goods only when they are movable and marketable, there is a lot of judicial enquiry into them. The issue of marketability is more or less well set at rest but the hitch of movability seems to be still pricking. Particularly, whether plant and machinery assembled at sight and embedded in the earth are (movable) goods or is not a major area that is to be addressed fully and satisfactorily. A close examination of these two concepts movability and marketability is necessary to understand excisability.

Goods are necessarily movable. There are moments of confusion which have drawn the attention of the judiciary as to what constitutes movability to attract excise levy. The word movable means capable of being moved or shifted from one place to another place. The word goods applies to those which can be brought to market for being bought and sold. It implies that the goods are movable. In *CIT v. N.C. Budharaja and Co.* (1993) S.C. it was held that the words manufacture/production are associated with movabilities - a dam or road is constructed - not manufactured or produced'. However, when an item emerges as a result of erection, installation or assembly attached to earth, it created controversy.

Case Laws



The following case laws should be helpful in drawing conclusions.

1. *Narve Tulaman Manufacturers Pvt. Ltd. v. CCE*, 1988 38 ELT 566 (SC)

The Supreme Court held that parts of weigh bridge cleared from factory and erected at site would be exigible to duty. However, it is important to note that the concept of goods and question of movability were not raised before the honourable court and this decision can not be said to be applicable to other cases when the concept of goods is the crux of the issue.

2. *Quality Steel Tubes (Pvt.) Ltd. v. CCE*, 1995 (75) ELT 17 (SC)

In this case, tube mill and welding machine were erected and installed in the premises and embedded in the earth for manufacture of steel and tubes and

pipes. The Supreme Court held that before duty could be levied, the article must be goods and should be capable of being brought to the market. The court also clarified that erection and installation of a plant could not be held to be excisable goods and that if such wide meaning is assigned, it would result in bringing within its ambit structures, erection and installation, which surely would not be in consonance with accepted meaning of excisable goods.

3. *Mittal Engg. Works (P) Ltd. v. CCE, (1996) S.C. ELT, 622*

Mono vertical crystallisers used in sugar factories for exhaustion of molasses of sugar were assembled, erected and attached to the earth as an immovable plant. The Supreme Court held that the plant when came into existence is immovable and hence not excisable. The court also refused to consider its earlier decision in *Narne Tulaman* case stating (that) "A decision can not be relied upon in support of a proposition that it didn't decide."

In pursuance of the above decision, the tribunal (CEGAT) has recently held in *Inconserve v. CCE, 2000 (120) ELT 638* that erection and commissioning of weigh bridge at sight after clearing from factory in parts is not manufacture.

4. *Siripur Paper Mills Ltd. v. CCE, 1997 (7) SCALE 594*

In this case the Supreme Court has slightly shifted from its earlier stand and held that paper making machine produced in parts, assembled, erected and attached to earth was goods manufactured and hence dutiable. In fact earlier, CEGAT in the same case held that the paper making machine was attached to the earth for operational efficiency and the whole purpose behind attaching the machine to a concrete base was to prevent wobbling of the machine and to secure maximum operational efficiency and also for safety. The Tribunal also held that the whole machinery could be dismantled and reassembled at another sight and hence the machinery was capable of being sold. The Supreme Court agreed with the ruling of the Tribunal.

But again the Supreme Court appears to have come back to its original position in *Triveni Engineering and Industries Ltd. and Another v. CCE and another, (2000) 120 ELT 273*.

5. *Triveni Engineering case*

In this case, turbo alternator assembled and erected at site was held to be not liable to duty as it would not satisfy the twin conditions of mobility and marketability for being called as goods. Also, held that marketability test required that the goods as such in a position to be taken to the market and sold. The turbo alternator would not satisfy the condition of marketability as it has to be separated into components, turbine and the alternator, to take it to the market, where it would not remain turbo alternator, and therefore the test would be incorrectly applied.

The following points can be drawn from the above and other decided cases.

- Moveability and marketability are associated factors of goods under excise.
- To be excisable, the goods must satisfy the twin tests of movability and marketability.
- Movability and marketability are a question of fact to be decided on merits.
- Erection of plant/machinery attached to earth is considered as immovable and not excisable.
- If any plant is erected/attached to earth superficially for safety, operational efficiency or simply to prevent wobbling, it can still be excisable goods. But it must be capable of being removed as such and not in parts.
- The burden of proof lies on the department where the question of movability or marketability arises.
- Movability is also an important test as nothing immovable can be manufactured.
- Test of movability is applied at the point and stage of manufacture and removal not at the time of its end use or utilisation. (*In Re Tisco Ltd.*)

MARKETABILITY

Marketability means saleability or suitability for sale. Various judicial pronouncements have amplified the significance of the concept.

Significance: Marketability is the acid test of excisable goods. Any event of manufacture resulting in goods must necessarily pass the test of marketability. It must be remembered that all goods are naturally movable but may not be marketable. Only those excisable goods manufactured are subject to levy of excise which are marketable. Since the prime purpose of manufacture is to sell, it is unthinkable of the manufacture of non saleable goods under the excise law. Right from DCM case, the apex court has been consistently holding that goods to be excisable, must be marketable.

The issue has drawn the attention of the apex court in a number of cases given below:



1. In *South Bihar Sugar Mills Ltd. v. U.O.I.* 1978 (2) ELT, the Supreme Court observed: the duty is levied on goods. As the Act doesn't define goods, the legislature must be taken to have used the word in its ordinary dictionary meaning. The dictionary meaning is that, to become goods, it must be something which can ordinarily come to the market to be sold and is known in the market.

Further said that mere theoretical possibility of marketability is not enough if the method is uneconomical and hardly likely to be employed by the trade.

2. In *Bhor Industries Ltd. v. CCE* 1989(40) ELT 280, the Supreme Court

examined the meaning of goods and clarified that as a first condition, goods must come into existence as a result of manufacture and for articles to be goods, the goods in question must be known in the market as such or these must be capable of being sold in the market as goods. In the instant case, the PVC crude films emerging as an intermediate product in the manufacture of leather garments is not marketable.

Recently, in ***United Phosphorous Ltd. (S.C.) 2000 117 ELT 529***, the Supreme Court rejected the contention of the department that the substances which were produced while manufacturing pesticides and insecticides were manufacture and held that they are not excisable as they are not identifiable in the market as goods.

3. ***Marketability is not necessarily an actual sale.*** The very fact was emphasized by the court in *CCE v. Ambalal Sarabhai Enterprises* 1989 (43) ELT-214, the court observed "Actual sale is not necessary. In cases where actual sale doesn't take place, it is for the department to prove that the goods are ordinarily saleable and market identifies them as goods.

Even a single buyer is enough to establish marketability if the sale is ordinary/regular - *APSEB v. CCE, Hyderabad S.C. (70) ELT 3*.

In the Instant case, Kerala State Electricity Board was the only buyer of cement poles from the AP State Electricity Board. Held, the poles are marketable goods.

The above decision has been followed by the Tribunal recently in *Dynamic Engineers* 2001 (128) ELT 101 (CEGAT). Dynamic Engineers have a tie up with the Indian Railways for the supply of GIR Joints. The Tribunal held that the conversion of rails into GIR joints is manufacture and the supply to railways, the alone buyer, vindicates marketability.

Even actual sale may not establish marketability if such sale is a stray, irregular extraordinary or distress sale. When a product emerging out of a process doesn't have a regular market, we may say that there is no marketability for the product. In *U.O.I. v. Aluminium Co. Ltd.* 1995 (77) S.C. ELT 268, dross and skimmings arising during manufacture of aluminium were held to be not goods as understood in commercial parlance even if they are sold and they fetch some price. Again in *CCE v. TISCO* 2004 ELT 386 the Supreme Court held that zinc dross & flux skimmings is waste and not manufacture. The court reiterated that everything that is sold is not necessarily marketable.

Intermediate goods, captively consumed goods, by-products, sub standard goods, waste and scrap are all goods if they are marketable at the stage of their production. They become excisable if they are specified under Central Excise Tariff Act, 1985. Intermediate goods means goods produced at an intermediate stage before the final product is produced. e.g. Plastic produced prior to the manufacture of plastic furniture. If the plastic is in a condition to be recognised as a product in the trade circles and is marketable as such it becomes excisable if found in Central Excise Tariff Act, 1985.

If intermediate products are consumed in the same factory for further processing, such intermediate products are called capitively consumed goods. Capitively consumed goods are usually exempted from duty through a notification when the final product is

dutiable. For instance, in the above case, plastic is produced and reused in the same factory to produce plastic furniture. When the plastic furniture is dutiable, plastic used in the process will be exempt from duty. If the plastic furniture is exempt from duty, raw plastic may be dutiable.

Similarly, sub standard goods, by products, scrap and waste products are all goods if they are marketable. And they become excisable if they are specified in Central Excise Tariff Act, 1985. But they must come into existence as a result of production or manufacture.

In *Khandelwal Metal & Engg. Works v. U.O.I. 1985 (20) ELT-222 the S.C.* held that the scrap & waste arising out of a process is a district commercial product and hence dutiable.

Marketability: An item of excisability, must necessarily pass the test of marketability. Marketability means saleability. The test of marketability is also known as vendibility test.

- *Marketability doesn't necessarily mean actual sale, actual sale need not take place even an intermediate product or an item of captive consumption is excisable if it is marketable at its stage of manufacture.*
- *Any intermediate goods not saleable are not goods [United Phosphorous Ltd. case, S.C., 2000].*
- *Market may be any market or any place. Even the factory godown may constitute market [Thiru Arooran Sugars].*
- *Even a single buyer constitutes market [A.P.S.E.B. Hyderabad v. C.C.E & Dynamic Engineers, CEGAT, 2001].*
- *By-products, or waste products may also be goods, if they are marketable and mentioned in Central Excise Tariff Act, 1985, [K.C.P. Sugars & Thiru Arooran Sugars].*
- *Goods in SKD/CKD condition are also goods (SKD - semi knocked down - CKD- completely knocked down) i.e. goods produced in parts and assembled subsequently at the time of use e.g. computers, fans, cycles.*
- *Goods with transient or short shelf life are also goods if they can be ordinarily sold during their short life.*
- *Burden of proof on marketability lies on the Deptt. [Ambalal Sarabai].*
- *Marketability is a question of fact [Siripur Paper Mills S.C. supra].*
- *Mere mention in Excise Tariff is not a proof of marketability. It must be proved independently [Ion Exchange (I) Ltd. v. CCE 1999 ELT 746 (SC) 112].*

Conclusion: The basic test of marketability of an item is the **recognition in the market and its saleability is the final test.**

RELATED CONCEPTS OF GOODS UNDER CENTRAL EXCISE

(a) Goods v. Excisable Goods: As cleared already, goods means those items which are movable and marketable at the stage of their production/ manufacture.

Excisable goods means those goods specified in Central Excise Tariff Act and subject to duty. Certain goods specified in the Schedule I to Central Excise Tariff Act carry NIL rates. Those having nil rate are leviable goods and those having some rate of duty are also leviable goods. Even the nil rated goods, are excisable goods. Exempted goods, needless to say, are also excisable goods. So, excisability of an item is not based on its dutiability, rather it is based on its placement in the Schedule to the Tariff. Again mere mention in Tariff is not enough to make it excisable. The manufactured goods having marketability become excisable.

(b) Leviable Goods v. Dutiable Goods: All excisable goods having some rate of duty are leviable goods. But leviability does not mean dutiability. When leviable goods are fully exempted from duty by a notification under Section 5A, they become non-dutiable goods. Dutiable goods are those on which duty is finally payable. Hence, all dutiable goods are leviable goods and all leviable goods are not necessarily dutiable.

(c) Exempted Goods v. Nil Rated Goods: Exempted goods means goods exempted by a notification under Section 5A of the Central Excise Act. But goods removed under bond are not exempted goods. Exempted goods are basically leviable goods. Fully exempted goods may become dutiable at the time of removal if the exemption is withdrawn by that time. For example, in *Wallace Floor Mills Co. Ltd. v. CCE* 1989 (44) ELT 598, when the goods were manufactured and packed they were fully exempt from duty. At the time of removal of goods from factory, the exemption was withdrawn. The Supreme Court held that the goods are dutiable and hence duty is payable.

The above land mark ruling established the point that dutiability is finally determined at the time of removal and not at the time of manufacture though the taxable event is manufacture. In other words, rate of duty prevailing at the time of removal and not at the time of manufacture, is relevant.

But same is not the case with NIL rated goods. When goods carry nil rate at the time of manufacture, they continue to be nil and no duty is payable on them unless there is a subsequent change in the tariff rate. Subsequent change may have immediate effect by virtue of Provisional Collection of Taxes Act 1931.

Moreover, if there is a subsequent change in classification of goods in question after manufacture but before removal, the latest classification number applicable at the time of removal will be relevant, which may turn out to be favourable or unfavourable to the assessee.

(d) Non-dutiable Goods v. Non-excisable Goods: Fully exempted goods are non-dutiable goods and non-excisable goods are non-leviable goods. In case of fully exempted goods, the effective rate of duty is Zero (Tariff rate minus exempted rate is effective rate). The fate of dutiability of exempted goods is decided at the time of their removal. The nil rated goods' fate is predetermined at the time of manufacture itself. They normally continue to enjoy the privilege of being nil until and unless they are brought under some other classification carrying some rate of duty at the time of removal or a fresh levy was made after manufacture but before removal.

Non duty paid goods are different from non dutiable goods. They are goods removed clandestinely (secretly) without invoice to evade duty.

(e) Non excisable goods v. Nil rated goods: Non-excisable goods are those goods not in the Tariff Act. Nil rated goods are CETA specified goods carrying nil rate or they can be called as goods chargeable to nil rate of duty. While the non excisable goods cannot be made excisable with retrospective effect, they continue to enjoy the status of non excisability even at the time of removal. It means goods non-excisable at the time of manufacture will continue to be non-excisable till end and any change in their status after manufacture and before removal will not affect them.

Nil rated goods, on the other hand, are excisable goods. Goods chargeable to nil rate may become dutiable at the time of removal if there is change in the tariff rate after manufacture but before removal. This may happen either due to change in classification number or change in tariff rate. Such changes are normally brought forth through Finance Act or by using emergency power under Section 3 of Central Excise Tariff Act, 1985.

6.2(b) THE CONCEPT OF 'EXCISABLE GOODS'

Once it is established that something falls within the ambit of the term "goods" then the issue to be decided is whether it is also "excisable goods".

The term "excisable goods" has been defined in Section 2(d) of the Central Excise Act 1944. It says that the term "excisable goods" means "goods specified in the First Schedule and the Second Schedule to the Central Excise Tariff Act 1985 as being subject to a duty of excise and includes salt".

Explanation: "goods" includes any article material or substance which is capable of being bought and sold for a consideration and such goods shall be deemed to be marketable.

Now, this would mean that it is not as if anything which is sold or is saleable (and hence 'goods') is taxable under Central excise. It *should also be specified in the First Schedule and Second Schedule to Central Excise Tariff Act, 1985.*

The definition in Section 2(d) is specific to the effect that it is only goods spelt out in the Tariff as being *subject* to duty that can be considered to be excisable goods. This would mean that it is only till the stage when the duty liability is not discharged by actual payment, that the goods can be called 'excisable goods'. Once the duty is paid or the goods have been *subjected* to duty, they are *not* excisable goods. *In sum, excisability attaches itself to the goods only till the point of payment of duty. Duties paid goods are not excisable goods.* In fact, this criterion is more specifically brought out in the Customs Act, 1962. While defining the corresponding tax liability on goods viz., "imported goods", Section 2(25) of the enactment defines imported goods as those which are brought into India from a place outside India, and makes it very clear that the term "imported goods" does *not* include goods which have been cleared through Customs for home consumption. Goods coming from abroad and cleared by Customs may be foreign goods but they are not imported goods (for purposes of Customs Law). Similarly, goods

manufactured in India, once they are cleared from the factory on payment of duty may continue to be manufactured goods, but they are not excisable goods (for purposes of Excise Law).

The following points are relevant for excisable goods:

- *Nil duty paid goods are also excisable goods, though duty is not paid, they do not lose their excisability. The mere fact that rate of duty on an article is NIL by reason of an exemption notification would not make it non-excisable goods. [UOI v. Nandi Printers, 2001 S.C. 127 ELT 645].*
- *Only those goods mentioned in the Central Excise Tariff Act, 1985 are excisable if they are movable and marketable at the time of manufacture.*
- *Goods from scrap waste or intermediate products for captive consumption are also excisable goods if they are mentioned in Central Excise Tariff Act, 1985.*
- *Duty paid goods cease to be excisable goods as they have already been subjected to excise duty.*

CONCLUSION

A manufactured item should necessarily find a place in Central Excise Tariff Act, 1985, otherwise, it is not excisable. Electricity is goods and it is manufactured and is movable and also marketable. But it is not mentioned in Central Excise Tariff Act, 1985, so it is not excisable.

6.2(c) PRODUCTION, MANUFACTURE AND PROCESS DISTINGUISHED

Under excise, the taxable event is manufacture or production. Hence, examination of these two terms manufacture and production is useful.

Production is a natural process by which a product is brought into existence. Eg. Production of tobacco, iron ore, jute, flowers etc. Manufacture, on the other hand involves some artificial process which adds some more utility to the product, e.g. Tobacco is produced and cigarettes are manufactured, similarly, sugar cane is produced and sugar is manufactured. Thus, we can conclude that every manufacture is production and every production is not manufacture. The Supreme Court in *CIT v. N.C. Budharaja & Co.* AIR (1993) S.C. 2529 held that the word production has wider connotation than *'the word manufacture'*. ***Every manufacture can be characterised as production but every production need not amount to manufacture.'***

But it may be noted that under excise, manufacture is more relevant than production since many items of production are either not excisable or exempted from duty.

“Concept of Manufacture”

Once it is established that what comes up for assessment is actually ‘goods’, and furthermore, is ‘excisable goods’, it is still to be established that there has been a manufacture thereof. This is because Section 3 of the Act authorises levy and collection of excise duties only on excisable goods produced or manufactured in India. This takes us to the third concept viz., “manufacture”.

This concept has not been defined in specific terms by the Act, and this omission, (deliberate or otherwise) has given rise to a spate of disputes. Before these are taken up for examination, the statutory definition under Section 2(f) may be examined.

Section 2(f) of the Act provides an inclusive definition of the term by saying that manufacture “includes any process incidental or ancillary to the completion of a manufactured product” and which is specified in relation to any goods in the Section or Chapter Notes of the First Schedule to the Central Excise Tariff Act 1985 as amounting to manufacture or which in relation to goods specified in the third schedule to Central Excise Act 1944 packing repacking labelling or relabelling declaration or alteration of retail sale price or adoption of any other treatment on the goods to render the product marketable also amounts to manufacture.

Thus, the definition of manufacture u/s 2(f) is in three parts, namely:

- (i) Incidental or ancillary process to the completion of a manufactured product.
- (ii) Deemed manufacturing processes specified in Central Excise Tariff Act, 1985.
- (iii) In relation to goods specified processes specific goods under Schedule III of Central Excise Act, 1944.

In fact, for the Schedule III items, valuation scheme based on retail sale price (under Section 4A) is applicable.

The phrase “*incidental or ancillary to the completion of a manufactured product*” deserves to be examined. Manufacture of any product is through a series of manufacturing processes taking place in sequence. At a particular stage, after the necessary processes are completed, the product emerging may be *functional*. Nevertheless, a few more processes may be necessary to render the product *saleable*. As noted earlier, it is *saleability* which is the crucial criterion for deciding *excisability*. Hence, the processes which take place to render the product which is already functional to become one which is also saleable, are those which can be considered as “incidental or ancillary to the completion” of the manufactured product.

Example

To illustrate, a piece of steel furniture, say a cup board, while being manufactured in a factory, emerges at a stage when it can function as a cup board, though it is still to be given spray painting etc. In such a situation, painting is a process ancillary to complete the cup board as a manufactured product capable of being sold. Excise duty will be charged only after the painting process is completed.

JUDICIAL PRONOUNCEMENTS ON THE CONCEPT OF MANUFACTURE



In the absence of a specific definition of “manufacture” in the Act, resort has to be made to pronouncements made in various judicial forums where this concept came up for examination. Important pronouncement of various courts in this regard are as below:

Union of India v. Delhi Cloth and General Mills and others (ELT - 1977 - J. 199).

This is a landmark judgment of the Supreme Court which settled for all purposes the scope of the concept “manufacture” in Central Excise. The facts in brief were that the parties who were manufacturers of Vanaspati purchased groundnut and Til oil from the open market. The oils thus purchased were subjected to different processes to convert them into Vanaspati. While they were no doubt paying excise duty on Vanaspati, the department contended that when the basic oils were being subjected to a series of processes, they emerged at a particular stage as a product which can be constructed as “Vegetable Non-Essential Oil” (VNE), which would attract duty under a separate Tariff Item. In other words, in the department’s view, there was “manufacture” of V.N.E. Oil attracting excisability, before its further conversion into Vanaspati, attracting excisability once again.

A great deal of evidence was let in by either side, which was elaborately examined by the learned Bench. It reduced the issue to the simple one whether mere processing itself can be construed to be manufactured. On this, they cited a passage quoted in the Permanent Edition of “Words and Phrases” Volume-26 from an American judgement. The citation which has assumed tremendous import in all disputes pertaining to “manufacture” in Central Excise since then, (being frequently cited by either side to disputes) runs thus:

“manufacture implies a change but every change is not manufacture; and yet every change of an article is the result of treatment labour and manipulation. But something more is necessary and there must be a transformation; a new and different article must emerge having a distinctive name character or use”.

This succinctly explains what constitutes manufacture. Manufacture implies several processes, and in each of them, by working upon what one starts with, changes are no doubt introduced. Still, such changes alone would not by themselves tantamount to manufacture. For the changes to be considered as manufacture, what results after the change should have different name, different character or different use, as against what one started with.

On this reasoning, the Supreme Court held in the D.C.M, case that *mere processing of the basic oils did not tantamount to manufacture of VNE Oils*, since on the basis of detailed examination of evidence, it was held that for VNE Oil popularly marketed as refined oil, the essential ingredient was that they were deodorised. *On the contrary, in the cases before them, though substantial processes of purification of the basic oils had taken place, still they were not deodorised, before being converted into Vanaspati.* Hence, the learned judges held that there had been no transformation bringing in new name, character or use, and hence there was no manufacture as such.

What is process?

The term process has not been defined in the Act. The dictionary meaning of process is a continuous and regular action or succession of actions taking place or carried on in a definite manner and leading to accomplishment of some results. In the

context of excise, a process is an operation or activity which may or may not result in production/manufacture. Usually, there are series of operations which bring into existence an item with a distinct name, character or use. For example, series of processes culminate in the production of rice; viz., ploughing, watering, sowing seeds, transplantation, weeding and harvesting. With the final process of harvesting, paddy is produced and rice, from paddy. **Similarly, cotton is produced by some natural process and cloth is manufactured by artificial processes such as ginning, pressing, threading and so on. In both production and manufacture, certain processes are involved.**

For excise purpose, mere process is not enough to call it manufacture/ production. Such process/processes should bring into existence an excisable entity preferably with a distinct name, character or use. For instance, a log of wood is cut into pieces. Cutting is a process, but not manufacture. Furniture is made out of wood. The process is manufacture as it is a distinct excisable item. Hence, we can conclude that every manufacture/production is a process and not necessarily *vice versa*.

In *Empire Industries v. U.O.I.* 1985 (20) ELT 179 S.C. the honourable court observed 'Processing' is different from manufacturing and mere change or processing does not mean manufacture. Any process creating something else having distinctive name, character or use would be manufacture. In this case, the apex court held that processing grey fabrics by bleaching, dyeing, printing of fabric will amount to manufacture.

In *CCE v. Rajasthan State Chemical Works* - 1991 (55) ELT 444 S.C. The term process has come to be examined again. The apex court observed:

"Manufacture involves series of processes. Process in manufacture or in relation to manufacture implies not only the production but the various stages through which the raw material is subjected to change by different operations. Each step towards production would be a process in relation to the manufacture. A process is a manufacture when it brings out a complete transformation so as to bring new commercially different article or commodity."

The court in the instant case held that to be a process, no physical/chemical change is necessary. Even material handling is a process of manufacture.

A further process can be a manufacture even if the final product and the input fall under the same tariff.

Case: *Decorative Laminates v. CCE* (1996) 6 S.C.627. Duty paid commercial plywood was reprocessed to produce slip proof commercial plywood. The process is an application of PF resin on duty paid plywood under 100% heat and, pressure and coating it with wire mesh to make it slip proof commercial plywood. This product is used in body building or flooring. In fact both input and the final product fall under the same classification No. [44.08]. Held that slip proof commercial plywood is a manufacture resulting in a distinct product. The court based its decision in Laminated Packagings (P) Ltd.

Earlier, the same court in *Laminated Packaging (P) Ltd.* 1990 held that laminated kraft paper with polyethelene amounts to manufacture as kraft paper and laminated kraft paper are two distinct products.

Printing logos and names on the bottles is not manufacture as the basic character of bottles doesn't change and bottles are marketable even without printing. **[U.O.I, v. J.G. Glass Industries 1998 (97) ELT-5 S.C.]**

In the instant case commercially marketable bottles were manufactured in one division and the same were sent to another division for ceramic colour printing and logos with decoration. **The Supreme Court held that a process can amount to manufacture if the commodity had no commercial value but for the said process**, the bottles were already marketable even without printing. Hence, printing is not manufacture.

Filtration/Process of Purification is not manufacture if the process does not change the basic character of the commodity. Case: *Premji Hari Das v. MCB* 1997 (89) ELT 658 (Bom. H.C.).

Commercial grade (C.G.) castor oil was further filtered and purified to make it BPG (British Pharmacopia Grade) castor oil. The department contended that the conversion into BPG is a manufacture on the ground that it is used for medical purposes and also purchased by different customers.

The Bombay High Court rejected the contention and held that the product can not be differentiated on the ground of its end use. It is to be judged by its distinctiveness. In this process of filtration, only impurity is reduced and the castor oil is retaining its character even after the process. Hence, no manufacture.

The following processes have also been held as manufacture:

- *Conversion of fruit pulp/concentrate into ready to serve beverage or fruit drink.*
- *Stitching of cloth to make clothes.*
- *Recording of sound on duty paid magnetic cassette tapes (in fact this is a process enumerated under Note 7 to Chapter 85 and any process mentioned in Central Excise Tariff Act, 1985 is undisputedly a manufacture).*
- *Assembling of computers from duty paid bought out parts.*

The following are not manufacture:

- *Printing a name on film; crushing of boulders into small stones; cutting, testing, packing, printing, labelling, repacking; conversion of marble blocks into marble slabs/tiles; recharging of batteries; pulverising, cleaning washing etc.*
- *Grading, sorting, purifying, remodelling, repacking, upgrading, sizing, reconditioning, repairing etc; galvanizing/corrugation of steel and retreading of old tyres.*

Important Note: The above mentioned processes can invariably amount to manufacture if they have been specifically mentioned in Chapter Notes or Section Notes under Central Excise Tariff Act, 1985. Eg. Under Note 5 to Chapter 4, labelling, re-labelling and packing of dairy products amount to manufacture.

PROCESSES SPECIFIED IN CENTRAL EXCISE TARIFF ACT, 1985 AMOUNTING TO MANUFACTURE/DEEMED MANUFACTURE

The following processes will be 'deemed to be manufacture' and duty will be payable if the process is specified in Central Excise Tariff as 'amounting to manufacture'.

'In case of dairy products like milk, cream, butter and cheese, labelling or re-labelling of containers and re-packing from bulk packs to retail packs or application of any other treatment to render the product marketable to the consumer shall amount to manufacture. [Note 5 to Chapter 4].

'Labelling' or 're-labelling' of containers and re-packing from bulk packs to retail packs of *pan masala* shall amount to manufacture. [Note 7 to Chapter 21].

'Labelling' or 're-labelling' of containers and re-packing from bulk packs to retail packs of *natural or artificial mineral waters* shall amount to manufacture. [Note 2 to Chapter 22].

'Labelling' or 're-labelling' of containers and re-packing from bulk packs to retail packs of organic chemicals shall amount to manufacture. [Note 11 to Chapter 29].

'Labelling' or 're-labelling' of containers and re-packing from bulk packs to retail packs of *colouring matter* shall amount to manufacture. [Note 3 to Chapter 32].

'Labelling' or 're-labelling' of containers and re-packing from bulk packs to retail packs of *perfumes, beauty preparations and preparations for use on the hair* shall amount to manufacture. [Note 4 to Chapter 33].

'Labelling' or 're-labelling' of containers and re-packing from bulk packs to retail packs of soaps, waxes etc. shall amount to manufacture. [Note 6 to Chapter 34].

'Addition to chemicals and other ingredients, Labelling or re-labelling of containers and re-packing from bulk packs to retail packs or any other treatment to render the product marketable in case of *insecticides, gums, artificial graphite* shall amount to manufacture. [Notes 2 and 5 to Chapter 38].

'Bleaching, mercerizing, dyeing, printing, twisting, texturising, doubling etc. to

- (a) yarn of wool [Note 3 to Chapter 51]
- (b) cotton fabrics [Note 3 to Chapter 52]
- (c) mono-filaments [Notes 3 and 4 to Chapter 54]
- (d) synthetic woven fabrics [Note 4 to Chapter 55]
- (e) special woven fabrics, tufted textile fabrics; lace and embroidery [Note 8 to Chapter 58]
- (f) knitted or crocheted fabrics [Note 4 to Chapter 60]

shall amount to manufacture.

Drawing or re-drawing of tubes, pipes of iron or steel shall amount to manufacture. [Note 3 to Chapter 73].

'In case of glass mirrors, glass bottles, glass envelopes, glass shells, clock or watch glasses, glass beads etc. process of printing, decorating or ornamenting shall amount to manufacture. [Note 5 to Chapter 70].

'Recording of sound or other phenomena on audio or video tapes shall amount to manufacture. [Note 7 to Chapter 85].

'Building a body or fabrication of structure on chassis shall amount to manufacture [Note 3 to Chapter 87, added by the Budget 2001].

'In relation to product of tariff item 2106 90 30, the process of *adding or mixing* cardamom, copra, menthol, spices, sweetening agents or any such ingredients, other than lime, katha or tobacco *to betel nut* in any form shall amount to 'manufacture'. [Note 6 to Chapter 21].

Conclusion: Manufacture is the focal point in determining levy of excise duty. There are two pronged approaches to find out whether a process is a manufacture or not. One, where the process is bringing into existence any product with a distinctive name, character or use, (as per judicial rulings) it is manufacture. Second, if the process is not manufacture as per the above test, then look up the chapter notes and section notes for processes deemed to be manufacture. If a process is not manufacture under either of them as above, make sure, there is no levy - as there is no manufacture. Again, there may be manufacture, still there may not be any levy when the product is not marketable; because manufacture and marketability are essential ingredients of goods to attract levy of excise duty.

Burden of Proof: When the process is not covered by Central Excise Tariff Act, 1985, the burden of proof that the process is manufacture, is on the Department.

Process amounting to Manufacture or not amounting to manufacture:

1. [CCEx vs. *Alok Enterprises* (2010) 259 ELT 333 (Bom.)]:

Purification and filtration done to make product hydrochloric acid and sulphuric acid marketable in the international market amounts to "manufacture". Such process was incidental or ancillary to manufacture of a marketable product.

2. [*Indian Cine Agencies vs. CIT* (2009) 233 ELT 8(SC)]:

Conversion of Jumbo rolls of Protographic films into small flats and rolls in the desired sizes amounts to manufacture.

3. CCEx vs. *Bencee Ltd.* (2010) 256 ELTA 16 (SC):

Process of slitting and cutting of steel coils to produce steel sheets and polyester films, which are used for the purpose of lamination, as the resultant product was not having different character therefore not amounts to manufacture.

4. Process of drawing or redrawing a bar, rod, wire rod, round bar or any other similar article into bright bar would amount to manufacture, i.e. Process of galvanization.
5. Process of converting ores into concentrate and process of refining of ore bar will amount to manufacture.

6.2(d) CONCEPT OF "MANUFACTURER"

This concept has also not been defined specifically in the statute, which however provides an inclusive definition under **Section 2(f) which runs thus: "manufacture" shall be construed accordingly and shall include not only a person who employs**

hired labour in the production or manufacture of excisable goods but also any person who engages in their production or manufacture on his own account”.

This inclusive definition identifies following types of parties who can be considered as manufacturers. Which are:

(a) Those who personally manufacture the goods in question on their own account.

(b) Those who get the goods manufactured by employing hired labour.

It is well known that sub-contracting, utilisation of facilities of ancillary units etc. are being increasingly resorted to even by major industrial units and the motivation in all such cases need not necessarily be dodging excise levies. In fact, even large public sector undertakings such as B.H.E.L. farm out production to a number of Small Scale Units, though it should not be difficult for them to manufacture those goods themselves. They do so as a matter of public policy, which is to encourage the growth of small entrepreneurs. However, there are cases where the motives may not be that honourable.

Excise department has given substantial duty concessions to the small scale sector, which reaches even to the level of no duty being charged on goods manufactured by the small scale units upto prescribed limits. Large scale manufacturers, at times, utilise this facility to avoid excise duties. It is done by supplying almost all the inputs, specifications, etc. to the small scale units, and at times even going to the extent of supervising the production by the small scale units. The goods are manufactured by the Small scale units and even the brand name of the other party (supplier of inputs, specifications etc.) affixed thereon. The goods are cleared at the concessional rate, and if the clearance is within the prescribed limits, even duty free and to that extent the ultimate price can be lesser or, in a sellers' market, the profit margin may be more. The goods are subsequently marketed by the large scale units (supplier of inputs) which stands to benefit substantially by such devices.

These matters have given rise to considerable litigation and a few important judgements in this context are as below:



(a) *Shree Agency v. S.K. Bhattacharjee & Others (1972 SC 780 AIR)* — The party, a firm dealing in textile goods, was supplying

cotton yarn to several powerloom units for conversion into fabrics on job-charge basis. Though the yarn was contended to be sold by Shree Agency to the powerloom units and the fabrics purchased back, with documentary evidence being fabricated for purposes of establishing the contention, the Department was able to prove that there was no sale as such, either way. The Supreme Court held that

Shree agency was the manufacturer, and was liable to pay duty on the fabrics which it got manufactured through independent powerloom units.

(b) *Ujagar Prints v. U.O.I 1989 (39) ELT 493 (S.C.)* — In this case, the S.C. has decided the core issue of valuation of goods manufactured by the job worker, while deciding that the job worker is the manufacturer and not the raw material supplier or brand owner. The Ujagar Prints were doing the process of manufacture on the materials supplied by another company. After finishing the job, the finished products were being sent back by Ujagar Prints and charging certain amount agreed upon. The charges of the processor included the processing profits. It was held that Ujagar Prints is

the manufacturer and the value of goods include the processor's charges. Justice Sabya Sachi Mukharji observed:

"Duties of excise are imposed on production or manufacture of goods and are levied upon the manufacturer or the producer in accordance with the relevant rules. This is quite independent of the ownership of goods."

In *M.M. Khambhattwala* case, the Supreme Court followed the principle in *Ujagar Prints* and observed that the house ladies who manufacture Dhoop and Agarbatti at home are manufacturers as there is no supervision or control over them by the raw material supplier.

- (c) **The Supreme Court of India has reiterated its earlier stand in *Ujagar Prints case in Pawan Biscuits Co. Ltd. v. CCE, Patna 2000, (120) ELT 24, SC*.** In this case, Pawan Biscuits was making biscuits for Britannia. Britannia was supplying raw material, recipe and packing materials. The product was being manufactured strictly according to Britannia's specifications. They were being sold under the brand name of Britannia. The Supreme Court held that Pawan Biscuits is the manufacturer and not Britannia Industries.

From the *Ujagar's* case and also from the other judicial pronouncements, the job of ascertaining the manufacturer so as to collect duty from him has become less complex. As already observed earlier, there is no difficulty in locating the manufacturer when goods are directly manufactured by himself or through hired labour in the premises of the owner of the goods. The difficulty is with those borderline cases where goods are delivered for job work or further process by another person especially when that another person happens to undertake the process of manufacture of final product. In such cases the basic test of relationship is applied to establish as to who is the manufacturer.

TESTS OF A MANUFACTURER

I. Relationship Test: If the relationship between the person getting the work done (through others) and the person who actually does is master-servant relationship or principal - agent relationship, then it is a case of manufacture through hired labour. If, on the other hand, the person who actually manufactures is *independent*, then he himself is the manufacturer. It is a case of principal to principal relationship *and not* of principal agent. In the first cited case of *Shree Agency*, the company maintained that the loom operators were independent processors but the department established that they were agents of the raw material suppliers as they were not even maintaining the accounts.

II. Profit Test: If the manufacturing profit is enjoyed and retained by the person who actually undertakes the process of manufacture, then he is surely independent and he is the actual manufacturer liable to pay excise duty. The profit test in fact is corollary to the test I, which further corroborates the relationship test.

Ordinarily, the following are not manufacturers —

Raw Material supplier: *If the raw material is supplied on principal to principal basis, (e.g. Bata Ltd. supplies raw material to job workers) the supplier is not manufacturer though he has a right to reject the goods.*

Brand Owner: *If the brand owner has no control over the manufacturing process/parties, he cannot be treated as manufacturer, even if he had supplied raw material and the manufacture is under his brand name [Basant Industries, Kanpur, S.C.].*

Raw material supplier is manufacturer if the manufacturer is either a dummy manufacturer or is the agent of the raw material supplier (Shree Agency).

Supplier of concentrates etc. *under franchise agreement is not a manufacturer and the bottling company is the manufacturer (Puna Bottling Co.).*

Person Supplying *raw material to produce drugs though having licence to produce is not the manufacturer. Person who actually manufactures drugs is the manufacturer.*

Labour contractor supplying labour is not the manufacturer *for the goods manufactured by the labour supplied by him under Contract Labour (Regulation & Abolition) Act, 1970.*

Conclusion: Whether the person, be it a raw material supplier or brand owner etc. is a manufacturer or not, is a question of fact. It depends upon - the type of relationship he holds with the person through whom he gets the work done (ii) the type of financial arrangement he has with such person.

He may exercise control over the quality and quantity of the production and still he may not be the manufacturer as the ultimate test is the enjoyment of profit. The burden of proof lies on that brand owner etc. to prove that he is not the manufacturer. Since the duty levied is collected from the manufacturer, it is necessary to identify the real manufacturer.

UOI v. Ahmedabad Electricity Company Ltd. 2003 ELT 3 (S.C.) (158)

Cinder - an unburnt/partly burnt pieces of coal in boiler and furnaces in thermal power plants is not a manufactured product. Cinder, a coal of inferior quality is used as a fuel and not as raw-material.

An item to be called as excisable should pass the tests of manufacture and marketability. Mere listing in the schedule to CETA is not enough.

Use of an item as fuel cannot be part of manufacturing activity in relation to end product. In producing cinder, no manufacturing process is involved.

CCE v. Kapri International (P) Ltd. 2002 (142) ELT (S.C.)

Manufacture and Dutiability:

Issues involved: (i) Whether cutting cotton fabrics from running length into small pieces such as bed sheets, table cloths, napkins and pillow covers amounts to manufacture ? (ii) Whether duty paid raw material (cotton fabrics in this case) and final products (pillow covers, napkins etc.) falling under same tariff item can be subjected to multiple levy.

The Honourable Supreme Court held that by cutting the cotton fabrics from running length into small pieces and giving them a definite required shape to form new articles like, bed sheets, bed spreads, table clothes etc, the respondent has produced a new commodity which has a definite commercial identity in the market. [Hence, it amounts to manufacture.]

On the question of dutiability the court observed that the mere fact that the material from which the new goods are manufactured, has suffered duty under a particular tariff item, that does not exclude the finished product from being exigible to fresh duty if the tariff Act provides for it. In the instant case, though the cotton fabrics had suffered duty under tariff item, the Tariff Act has made bed sheets, pillow covers etc., also dutiable under the very same tariff item, therefore the respondent is liable to pay duty on bed sheets etc. also manufactured by it.

NOTE: The S.C. relied on its earlier decision in *Laminated Packagings (P) Ltd., 1990.*

Nandi Printers (P) Ltd. – SC, 2001

Held that the goods remain excisable, even if they are fully exempted from duty (Note: SC, in Wallace Flour Mills Company Ltd., held that if goods are fully exempted from duty on the date of manufacture, and exemption is withdrawn by the date of removal, the goods become dutiable). Because, relevant date for determining the dutiability is the date of removal.

LATEST CASES ON MANUFACTURE AND GOODS

[CCEx. Vs. Mehta & Co. (2011) 264 ELT 481 (SC)]:

Furniture refers to desks, table and chairs etc. and is different from fixtures that are attached to earth/ground/walls. Furniture cannot be regarded as immovable property. Therefore, furniture manufactured at customers site is movable and is liable to excise duty.

Cipla Ltd. 2008 (S.C.)

The pharmaceutical company is manufacturing medicines. Incidentally a substance called BENZYL Methyl Sali cylate (BMS) is being produced but the company declared that the substance is non excisable because it is not marketable.

Earlier, the tribunal held that the goods are marketable on the ground that chemical weekly drug directory mentioned that BMS as intermediate product.

On appeal by the company, the Supreme Court held that the BMS is not marketable as the department failed to prove its marketability.

M/s. Prachi Industries, [S.C.] 2008

Supreme Court held that the process of swaging undertaken by the assessee on swaging machine on duty paid MS tubes, amount to "manufacture".

In the present case the rotary swaging machine with different dies therein imports a change of lasting character to the plain pipe or tube by use of dies.

Board of Trustees, Port Trust v. CCE, 2007 (S.C.)

Cement concrete armour units for installation of break waters in the outer harbour for keeping the waters calm. Held that the concrete blocks are not marketable as there is no evidence that the goods are capable of being sold in the market.

Mahavir Aluminium Ltd. 2007 (S.C.)

Held that conversion of aluminium scrap in gots and other alloying material by process of melting into aluminium billets is a manufacturing process.

Hindustan Poles Corporation v. CCE 2006 (S.C.)

Mere joining of three pipes – one with the other of different dimensions to obtain a desired length is not manufacture. Such joining by no stretch of imagination can be brought within the category of manufacture.

CCE v. Pan Pipes Resplendents Ltd. 2006 (193) ELT 129 (SC)

Drying and colouring of duty paid plain glazed ceramic tiles into decorated glazed tiles is not manufacture as there is no new distinct commercial commodity comes into existence.

Kores India v. CCE (2004) ELT 7(SC)

Conversion of jumbo reels of ribbons into spools form to be used for type writers and Telex machines is 'manufacture' as new and distinct product emerges. In this case the Supreme Court upheld the decision given by the Tribunal.

Tata Consultancy Services v. State of Andhra Pradesh (2004) 141 Taxman 132 (SC)

A 5 member bench of Supreme Court held that branded software is goods. The same view has been upheld by Supreme Court in *Bharat Sanchar Nigam Ltd. v. UOI* (2006) 3 SCC1.

6.3 CLASSIFICATION OF GOODS

Classification is the process by which identification of excisable goods can be made. Under the central excise, the goods are identified by their code numbers called as classification numbers. Ascertaining the classification number is necessary to:

- Determine *excisability* of the goods manufactured;
- Finding out *rate of duty* applicable to such excisability;
- Establish *dutibility* by checking up whether any exemption is available under Section 5A of Central Excise Act, 1944, or any new levy or increase of duty is there under Section 3 of Central Excise Tariff Act, 1985;
- Proper classification of goods ensures smooth functioning and avoids disputes.

Note: Dispute on classification is a question of law, and any appeal from CESTAT lies directly to the Supreme Court.

Classification — Salient Features

- Classification is based on eight digit system. First two digits represent Chapter number, next two digits, Heading number and the last two digits show the Sub-heading number of the goods in question.
- *Chapter No. and Heading No. may be common but the sub-heading is unique.*
- Schedule 1 of the Central Excise Tariff Act, 1985 as amended with effect from 28.3.2005 has four columns viz: (i) Tariff Item (ii) Description of goods (iii) unit (iv) rate of duty.

- Rate of duty in the last column may be specific i.e. on quantity or as % age (*ad valorem*).
- The goods are so grouped that they are classified beginning with raw-material and ending with finished goods under the same Chapter.
- There are 20 Sections in the Schedule. Each Section is divided into a number of Chapters and each Chapter is further divided into Headings and Sub-headings.
- There are Section notes and Chapter notes to enable better understanding and proper application which have *binding effect*.
- There are also rules provided for interpretation in case of need. If the rules cannot be applied successfully, then the principles evolved by the courts may be resorted to.
- In case of dispute over correctness of classification No., *the burden of proof* is on the department. [*Hindustan Ferodo Ltd. 1997, S.C.*]

Rules for Interpretation

Classification of goods in this Schedule shall be governed by the following principles:

1. The titles of Sections, Chapters and Sub-Chapters are provided for ease of reference only; for legal purposes, classification shall be determined according to the terms of the headings and any relative Section or Chapter Notes and provided such headings or Notes do not otherwise require, according to the following provisions.
2. (a) Any reference in a heading to an article shall be taken to include a reference to that article incomplete or unfinished, provided that, as presented, the incomplete or unfinished article has the essential character of the complete or finished article. It shall also be taken to include a reference to that article complete or finished (or falling to be classified as complete or finished by virtue of this rule), presented unassembled or disassembled.
- (b) Any reference in a heading to a material or substance shall be taken to include a reference to mixtures or combinations of that material or substance with other materials or substances. Any reference to goods of a given material or substance shall be taken to include a reference to goods consisting wholly or partly of such material or substance. The classification of goods consisting of more than one material or substance shall be according to the principles of rule 3.
3. When by application of rule 2(b) or for any other reason, goods are, *prima facie*, classifiable under two or more headings, classification shall be effected as follows:
 - (a) the heading which provides the most specific description shall be preferred to headings providing a more general description. However, when two or more headings each refer to part only of the materials or substances contained in mixed or composite goods or to part only of the items in a set put up for retail sale, those headings are to be regarded as equally specific in relation to those goods, even if one of them gives a more complete or precise description of the goods.

- (b) mixtures, composite goods consisting of different materials or made up of different components, and goods put up in sets for retail sale, which cannot be classified by reference to (a), shall be classified as if they consisted of the material or component which gives them their essential character, insofar as this criterion is applicable.
 - (c) when goods cannot be classified by reference to (a) or (b), they shall be classified under the heading which occurs last in numerical order among those which equally merit consideration.
4. Goods which cannot be classified in accordance with the above rules shall be classified under the heading appropriate to the goods to which they are most akin.
 5. In addition to the foregoing provisions, the following rules shall apply in respect of the goods referred to therein:
 - (a) camera cases, musical instrument cases, gun cases, drawing instrument cases, necklace cases and similar containers, specially shaped or fitted to contain a specific article or set of articles, suitable for long-term use and presented with the articles for which they are intended, shall be classified with such articles when of a kind normally sold therewith. This rule does not, however, apply to containers which give the whole its essential character;
 - (b) subject to the provisions of (a) above, packing materials and packing containers presented with the goods therein shall be classified with the goods if they are of a kind normally used for packing such goods. However, this provision does not apply when such packing materials or packing containers are clearly suitable for repetitive use.
 6. For legal purposes, the classification of goods in the sub-headings of a heading shall be determined according to the terms of those sub-headings and any related sub-heading Notes and mutatis mutandis, to the above rules, on the understanding that only sub-headings at the same level are comparable. For the purposes of this rule the relative Section and Chapter Notes also apply, unless the context otherwise requires.

General Explanatory Notes

1. Where in column (2) of this Schedule, the description of an article or group of articles under a heading is preceded by “-”, the said article or group of articles shall be taken to be a sub-classification of the article or group of articles covered by the said heading. Where, however, the description of an article or group of articles is preceded by “--”, the said article or group of articles shall be taken to be a sub-classification of the immediately preceding description of the article or group of articles which has “-”. Where the description of an article or group of articles is preceded by “---” or “----”, the said article or group of articles shall be taken to be a sub-classification of the immediately preceding description of the article or group of articles which has “-” or “--”.
2. The abbreviation “%” in column (4) of this Schedule in relation to the rate of duty indicates that duty on the goods to which the entry relates shall be charged on

the basis of the value of the goods fixed, defined or deemed to be, as the case may be, under or in sub-section (2) read with sub-section (3) of section 3 or section 4 or section 4A of the Central Excise Act, 1944, the duty being equal to such percentage of the value as is indicated in that column.

Additional Notes

In this Schedule,—

- (1) (a) “heading”, in respect of goods, means a description in list of tariff provisions accompanied by a four-digit number and includes all sub-headings of tariff items the first four-digits of which correspond to that number;
- (b) “sub-heading”, in respect of goods, means a description in the list of tariff provisions accompanied by a six-digit number and includes all tariff items the first six-digits of which correspond to that number;
- (c) “tariff item” means a description of goods in the list of tariff provisions accompanying either eight-digit number and the rate of the duty of excise or eight- digit number with blank in the column of the rate of duty;
- (2) the list of tariff provisions is divided into Sections, Chapters and Sub-Chapters;
- (3) in column (3), the standard unit of quantity is specified for each tariff item to facilitate the collection, comparison and analysis of trade statistics.

Cases under Classification



1. *Uncle Chips Co. Ltd. v. CCE, Ghaziabad*; 2001 (134) ELT 549, CEGAT.

The issue before the Tribunal was whether the roasted peanuts & moongfali masala majedar - both preparation of nuts - are classifiable under Chapter 8 or Chapter 20, the assessee maintained that these fall under Chapter 8 attracting nil rate but the department contended that these fall under Chapter 20 attracting 16%.

2. *Shree Baidyanath Ayurved Bhavan Ltd. v. C.C.E., Nagpur* [1996 (83) ELT 492 (SC)]

The Hon'ble Supreme Court has held that:

“Dantamanjan Lal (Tooth powder) is not a medicine (Ayurvedic) - Not classifiable as medicine. Hence, not eligible for exemption under notification No. 62/78-C.E.”

“Medicine is ordinarily prescribed by a medical practitioner and it is used for a limited time and not every day unless it is so prescribed to deal with a specific disease like diabetes”.

“Scientific and technical meaning of the term and the expressions used in the tax laws like Excise Act, not to be resorted - Goods to be classified according to the popular meaning attached to them by those using the product.”

The Hon'ble Tribunal in case of *Alpine Industries v. CCE, Delhi* [1997 (92) ELT 53 (Tribunal)] have stated that "The fact of manufacture of an item under license under the Drugs and Cosmetics Act is no guarantee that it is a medicament.

Earlier in *Richardson Hindustan Ltd.* [1988 (35) ELT 424 (Tribunal)].

Hon'ble CEGAT has classified Vicks Vaporub as Ayurvedic Medicine and there is no definition of any word in the relevant statute, the word must be construed in the popular sense i.e. the meaning as understood by the people conversant therewith."

3. Classification of Spares or Accessories - Car Seat Covers

Many times the manufacturer is in dilemma whether his finished goods would be held as spares or components or accessories and how the classification should be done if the goods are manufactured with a specific intended purpose for example, seat covers of car seats. Look at the following decision.

In case of *Guru Overseas Pvt. Ltd. v. CCE, Delhi 2000* (120) ELT 209 (Tribunal) held "Car Seat Covers - whether of "Leather" or "Textile" are accessories and classifiable under Chapter Sub-heading 8708.00. The Tribunal followed the ratio of CEGAT judgement in the case, *Kirloskar Pneumatic* reported in 1991.

Assessee in the instant case is a manufacturer of car seat covers both of leather and cloth. He classified the leather covers under articles of leather under heading 4201.90. He also manufactured covers of textile and classified them under 6301.01 titled blankets, Traveller's rugs.

The department argued that these are integral part of car seats and proposed the classification of both the goods under 9401.00 (Seats). The Tribunal held that the additional covers for seats are accessories classifiable as 'parts and accessories of the motor vehicles'.

4. Other Cases: 1994 (74) ELT 233 (CAL) *Hindalco Industries v. Collector of Customs, Bombay*

"Onus is on Department to justify classification of goods under a heading attracting higher rate of duty"

5. *Plastrulon Processors Ltd. v. CCE, 2002* (139) ELT 148 (T)

The Tribunal held that –

- (a) Reinforcing carbon steel pipe with PTFE tube to give anti-corrosive characteristics, resulting into emergence of new product namely, 'carbon steel pipe lined with plastic', amounts to manufacture.

Note: The court applied and followed the twin tests laid down by the Supreme Court in *U.O.I. v. JG Glass Industries Ltd.* 1998 (97) ELT 5 (SC)

Twin Tests:

- Different commercial commodity should come into existence and the original commodity should cease to exist.
- But for the process, the final product shall not have full commercial value. In other words, carbon steel pipe lined with plastic' can be used for the purpose which was not possible but for the process.

- (b) For determining the classification of a composite product (carbon steel pipe lined with plastic), the lining material of plastic cannot be taken as carrying essential character of the product. Though the total cost of the plastic materials more than 80% of the total cost, the value is irrelevant. The plastic tube is used in the composite product only to reinforce the Carbon Steel Pipe so that it gets the characteristics of Anti-corrosion Tube. The essential character of the product is conveying the liquid material and not the anti-corrosion speciality.

Notes:

1. Rule 3 (b) of Interpretative Rules under Central Excise Tariff Act, 1985 was sought to be applied in the instant case.
 2. The ratio of Sprint RPG India Ltd. 2000 (116) ELT 6 given by the Supreme Court (which decided the essential character of a composite product on the basis of value) was refused to be applied in this case as the facts are different.
- (c) Department has power to review the Classification No. approved and adjudicated earlier under Section 35E of the Central Excise Act, 1944. It cannot be estopped from denying the earlier approval.

6. *Natural Health Products (P) Ltd. v. CCE, Hyderabad 2003 (158) ELT 257 (SC)*

Supreme Court Held that Vicks medicated cough drops and vicks vaporub throat drops are manufactured by using natural herbals by purifying them to pharmaceutical grade. In spite of refinement they do not become synthetic in nature. They are classifiable under 30.03.30 attracting nil rate and not classifiable under 3003.10.

Ayurvedic medicament even if patented in USA can still be an ayurvedic medicine if it has the characteristics of such medicine.

Since there is no definition of Ayurvedic medicine under Excise Laws, the common parlance test has to be applied to ascertain whether it is treated by the public as Ayurvedic medicine.

Note: Subheading 30.03.10 covers patent or proprietary medicaments other than those medicaments which are exclusively Ayurvedic, Unani Sidha or Homoeopathic attracting 15% of duty.

Miscellaneous topics under classification

When the classification is not possible even as per rules, guidelines provided by the courts must be referred to. The Courts have consistently held from time to time that:

Trade parlance test must be preferred to technical or dictionary meaning of the words. When trade parlance test fails, other options including BIS (Bureau of Indian Standards) classification may be tried.

Timing of classification

Procedures start with Classification. Classification of excisable goods must be done even before getting the registration. Again, leviability of goods is determined on the basis

of classification applicable at the time of manufacture. However, dutiability of goods is decided as per the rate of duty on the date of such removal.

Change of classification number

When there is a change in classification number after manufacture but before removal of goods, the latest classification number prevailing at the time of removal is to be applied. Even those goods attracting Nil rates at the time of manufacture may become dutiable at the time of removal due to the subsequent change in classification.

Classification is primarily the responsibility of the assessee. Proper classification avoids disputes and ensures smooth functioning. Any reckless venture into this is highly risky and it may attract show cause notices under Section 11A from the department.

Central Excise Tariff Act, 1985 has two schedules. Schedule I has all excisable goods and the duty leviable on them is called CENVAT.

Very few items, (8 Heading Nos.) reappear in Schedule II which attract one more duty called SED (special excise duty) which is in addition to CENVAT. The chapters given below have the goods attracting SED.

Note: SED is exempt with effect from 1.3.2006.

6.4 VALUATION OF GOODS UNDER CENTRAL EXCISE LAW

Goods are required to be assessed at the time of removal after levy of duty at the time of Manufacture. The assessment is made as per the rates specified in Central Excise Tariff Act, 1985. As we are aware, there are two Schedules under Central Excise Tariff Act. The duty levied under the First Schedule is called CENVAT and the duty under Second Schedule is SED (Special Excise Duty). If a manufactured item figures in only First Schedule, only CENVAT is levied.

Rates of Duty: Basically, there are two rates of duty levied under Central Excise Act, 1944; specific rates and advalorem rates. Specific rates are unit rates based on quantity. The base unit may be a kilogram, a centimeter, a quintal, a tonne and so on. Some of the goods and their respective rates are given below:

<i>Excisable Item</i>	<i>Base Unit</i>
Cigarettes	millimeter (Length)
Cement	Tonne (Weight)
Marble Slab	Square Metre (Area)
Sugar	Quintal (Weight)
Tea	Kilo (Weight)
Molasses	Tonne (Weight)

A very few items attract specific rates under excise law. The specific rates are easy and simple to understand and apply but, there are practical difficulties attached to them. It is not possible to fix rates for all the varieties of goods. They require frequent revision due to price fluctuations. That is the reason why *ad valorem* rates (i.e. percentage rates based on value of manufactured goods) are in vogue all over the world.

The ad valorem rates have the following advantages:

1. *They are flexible and elastic*
2. *They are scientific*
3. *They are convenient*
4. *They have in-built adjustability to price and quality variations.*

A very few items are valued on specific-cum-*ad valorem* rates e.g. Cigarettes are first assessed at specific rates under Central Excise Tariff Act, again they are valued on *ad valorem* rates as applied under Additional Duties of Excise (Goods of Special Importance) Act.

It may be noted that no item under Schedule II attracts specific rates.

From the above discussion, it is clear that most of the excisable goods are assessed on *ad valorem* basis. That means goods require valuation and on that value (Known as assessable value), duty amount is calculated at specified percentage rates. There are three methods of valuation under Central Excise Act, 1944:

1. Valuation based on Government notified values [Section 3(2)];
2. Valuation based on MRP (Maximum Retail Price) for the goods notified by the Government (Section 4A);
3. Valuation based on Transaction Value (T.V.) (Section 4)

Before discussing the above methods let us have a look at some of the duties levied under Excise.

<i>Name of the Act</i>	<i>Name of the Duty</i>
Central Excise Act, 1944	CENVAT and SED
Additional Duty of Excise (Goods of Special Importance) Act, 1957	Additional Duty on tobacco, Sugar etc.
Additional Duties of Excise (Textiles & Textile Articles) Act, 1978	Additional duty on textiles products
Finance Act, 2001 (Section 136)	National Calamity Contingent Duty on Cigarettes, Bidis & other tobacco products plus pan masala, pan parag etc.
Finance Act, 2004	Education cess
Finance Act, 2005	Surcharge under Section 85 as an additional duty of excise.
Finance Act, 2007	Secondary & Higher Education (SHE) cess

Notes:

- (1) AED (GSI) on all products has been exempted w.e.f. 1.3.2006
- (2) AED (T&TA) was abolished w.e.f. 9.7.2004.

- (3) AED (Tea & Tea Waste) levied under Section 157 of Finance Act, 2003 was abolished w.e.f. 1.3.2005.

6.4.1 Methods of Valuation

Excise duty is either specific duty or advalorem duty. The type of duty and the rate of duty applicable is mentioned in the Schedules to Central Excise Tariff Act, 1985. Most of the excisable goods are charged under **ad valorem basis**. As stated earlier, there are three methods of calculating assessable value under the excise laws when goods are valued under *ad valorem* basis.

Methods of Calculating Assessable Value::

- *Tariff values under Section 3(2) notified by Govt.*
- *MRP based values computed for the goods notified by the govt. under Section 4A.*
- *Transaction value under Section 4 where the assessable value under the above two methods is not applicable.*

Tariff Values: The Central Government is authorised to notify tariff values for certain excisable goods. The tariff value is the notional value. Where the tariff values are fixed under Section 3(2), neither transaction value nor MRP based value can be used for such goods. The following points are relevant for the tariff values:-

- The tariff values are fixed by Central Govt. by notification.
- A few goods are covered under this scheme.
- Different tariff values may be fixed for different products or different values for different manufacturers of same product.
- The values may be even different for different classes of buyers.

The main purposes for which the tariff values are fixed are to prevent undervaluation of certain goods and to mitigate litigation.

Basis of Fixation: The values may be fixed by the Government on the basis of (i) whole sale prices or (ii) average of such whole sale prices. Pan Masala packs below 10 grams are covered under tariff values and Pan Masala packs of 10 grams and above are covered under Section 4A [MRP based assessable values].

6.4.1(a) Valuation Based On MRP [Retail Sale Price] (Section 4A)

On 4th November, 1987, the Collectors' (Excise) Conference was held. It was suggested in the conference that retail price instead of wholesale price should form the basis of valuation for assessment of excise duty for such commodities which show a difference of more than 100% between the retail price and the wholesale price. The Board consequently, called for details of such commodities. It took nearly a decade to translate the proposal into a reality. The budget 1997 finally introduced the system. Section 4A was inserted in the Central Excise Act and the valuation based on retail price came into effect on 14th May, 1997. This novel concept of assessment of duty on consumer goods met with a thumping success. Even the litigation under this has been at a low ebb.

Under this scheme, Central Govt is authorised to notify certain goods sold in a

packaged form having MRP printed on them. The Legal Metrology Act 2009, requires the packaged commodities to bear the maximum retail price (MRP). Out of such packaged commodities, some of them have been notified by the govt. from time to time and such commodities notified by the govt. are valued under Section 4A of the Central Excise Act, 1944.

The notified goods should necessarily bear the MRP. The MRP declarations are statutorily required where the printing of MRP is statutory and not compulsory, or where the assessee prints the MRP voluntarily, such goods need not be valued under Section 4A even though the goods are notified by the Government for this purpose. The MRP is the basis for arriving at assessable value. Rates of abatement are notified by the Government. Rates of abatement may be different for different commodities.

The assessable value = MRP – Abatement value.

The amount of duty is percentage of duty mentioned in the Schedules to Central Excise Tariff Act.

Refrigerators under classification No.8418.10 carry abatement rate of 38% and they are specified only in Schedule I. Find out the amount of duty if the MRP of a refrigerator is ₹10,000 and rate of duty 8 %.

Solution: Assessable value is 62% of ₹10,000 i.e. ₹6,200. The amount of duty is 8% excise duty and cesses at 3%, will be 8.24% of ₹ 6,200.

6.4.1(b) Scope and Objects

Section 3(2) overrides Section 4 and Section 3(2) and Section 4A are mutually exclusive. Same goods are not subjected to tariff values as well as valuation under Section 4A. The main objectives of valuation are:

- To discourage the practice of manufacturers offering high margins to the retailers by printing higher MRPs.
- To augment revenue collections by levying duty on post removal expenditure like, advertisements, transportation, middle men's profits etc.
- To simplify the process of valuation finally to reduce litigation.

Section 4A overrides Section 4. It means transaction value cannot be adopted for the valuation of goods notified under Section 4A. [Section 4A(2)] [Bata India, 1999, CEGAT].

Even if the goods are manufactured by a job worker, the valuation of goods must be done under Section 4A only when the goods are notified under this section.

The application of MRP based valuation is subject to the following rules:

- *If a package contains different MRPs printed on it, highest of them must be taken for the purpose of valuation.*
- *If separate MRPs are printed on packages meant for sale in different places, each of such MRP is taken for the purpose of valuation and each such consignment is valued separately.*

The following acts of a manufacturer render the goods liable to confiscation.

- Removal of goods without MRP declaration.
- Declaration of a price which is not the sole consideration, Tampering, obliterating, or altering the printed MRP after removal of goods.

Note: The aforesaid acts are in particular, the first and the last are violations even under the Legal Metrology Act, 2009.

"**Retail Price**" under this section means the maximum price at which the excisable goods in packaged form may be sold to the ultimate consumer and includes all taxes local or otherwise, freight, transport charges, commission payable to dealers, and all charges towards advertisement, delivery, packing, forwarding and the like, as the case may be, and the price is the sole consideration for such sale.

Cases

Whirlpool of India Ltd. 2007 (S.C.) – Held that Refrigerator is a prepacked commodity and sale of refrigerator is a retail sale and hence assessable under Section 4A.

Kraftec Products Inc. 2008 (S.C.) – Multi Piece packets whose total weight is less than 10 grams are liable to be valued under Section 4 and not under Section 4A, even though they have been notified by the government under Section 4A.

Kraftec manufactures hair dye. It is packed in pouches each containing 3 gms. 3 pouches (sachets) are sold in one packet. The net weight of each pouch, as also the net weight of the commodity in 3 pouches and the maximum rate is printed on the pouches.

Note: As per Rule 34 of Packaged Commodity Rules, 1977, the retail packs below ten grams/10 ml. are exempt from printing MRP on them. Where MRP is not a statutory requirement, Section 4A can not be applied.

Jayanti Food Processing (P) Ltd. 2007 (S.C.) – Held that ice cream supplied in the four litre pack to hotels is a wholesale pack and not retail pack. As such, the goods have to be assessed under Section 4 and not Section 4A.

Vide department circular No. 873/11/2008 – dt. June 24, 2008, the department accepted the above decision.

6.4.1(c) Concept of Transaction Value

The law pertaining to determination of assessable value for excisable goods is contained in Section 4 of the Central Excise Act, 1944, supplemented by the Central Excise Valuation (Determination of Price of Excisable Goods) Rules, 2000. Section 4, as it exists now, has been introduced into the statute by an amendment made by the Finance Act, 2000, and brought into force w.e.f. July 1, 2000 on which date the Valuation Rules were also simultaneously brought into force.

Note: The substitution of the concept of assessable value from "Normal Wholesale Price" to "Transaction Value" has been made to make the valuation mechanism simple, user friendly and along commercially accepted lines. Besides, it has been termed as a move to facilitate the introduction of full-fledged VAT in place of CENVAT as introduced in Central Excise Law through Union Budget, 2000.

The current Section 4 closely follows the prescription regarding assessable value to be based on 'Transaction Value' in the first instance as in Section 14 of the

Customs Act, 1962. The Customs concept, in turn, is inspired by the Brussels Concept of Value i.e. the concept of assessable value in commodity taxation, conceived and devised by the Customs Co-operation Council (CCC) Headquartered in Brussels, Belgium. It is noteworthy that it is the CCC which is the author of the Harmonised System Nomenclature which forms the basis of the Excise and Customs Tariffs recently introduced in India.

6.4.2 Procedure for Fixation of Value under Section 4

Section 4 of the Central Excise Act, 1944 as substituted by Section 94 of the Finance Act, 2000 (No. 10 of 2000), which has come into force the 1st day of July 2000, reads thus,

“4.(1) Where under this Act, the duty of excise is chargeable on any excisable goods with reference to their value, then, on each removal of the goods, such value shall:

- (a) in a case where the goods are sold by the assessee, for delivery at the time and place of the removal, the assessee and the buyer of the goods are not related and the price is the sole consideration for the sale, be the transaction value;
- (b) in any other case, including the case where the goods are not sold, be the value determined in such manner as may be prescribed.

**Explanation—*For the removal of doubts, it is hereby, declared that the price-cum-duty of the excisable goods sold by the assessee shall be the price actually paid to him for the goods sold and the money value of the additional consideration, if any flowing directly or indirectly from the buyer to the assessee in connection with the sale of such goods and such price-cum-duty excluding sales-tax and other taxes, if any actually paid, shall be deemed to include the duty payable on such goods.

- (2) The provisions of this section shall not apply in respect of any excisable goods for which a tariff value has been fixed under Sub-section (2) of Section 3.
- (3) For the purpose of this section:
 - (a) “**assessee**” means the person who is liable to pay the duty of excise under this Act and includes his agent;
 - (b) **persons shall be deemed to be “related” if:**
 - (i) they are inter-connected undertakings;
 - (ii) they are relatives;
 - (iii) amongst them the buyer is a relative and a distributor of the assessee, or a sub-distributor of such distributor; or
 - (iv) they are so associated that they have interest, directly or indirectly, in the business of each other.

Explanation: In this clause:

- (i) “**Inter-connected undertakings**” means two or more undertakings which are interconnected with each other in any of the following manners, namely:—
 - (A) if one owns or controls the other;

- (B) where the undertakings are owned by firms, if such firms have one or more common partners;
- (C) where the undertakings are owned by bodies corporate,—
 - (I) if one body corporate manages the other body corporate; or
 - (II) if one body corporate is a subsidiary of the other body corporate; or
 - (III) if the bodies corporate are under the same management; or
 - (IV) if one body corporate exercises control over the other body corporate in any other manner;
- (D) where one undertaking is owned by a body corporate and the other is owned by a firm, if one or more partners of the firm,—
 - (I) hold, directly or indirectly, not less than fifty per cent. of the shares, whether preference or equity, of the body corporate; or
 - (II) exercise control, directly or indirectly, whether as director or otherwise, over the body corporate;
- (E) if one is owned by a body corporate and the other is owned by a firm having bodies corporate as its partners, if such bodies corporate are under the same management;
- (F) if the undertakings are owned or controlled by the same person or by the same group;
- (G) if one is connected with the other either directly or through any number of undertakings which are inter-connected undertakings within the meaning of one or more of the foregoing sub clauses.

Explanation 1.— For the purposes of this clause, two bodies corporate shall be deemed to be under the same management,—

- (i) if one such body corporate exercises control over the other or both are under the control of the same group or any of the constituents of the same group; or
- (ii) if the managing director or manager of one such body corporate is the managing director or manager of the other; or
- (iii) if one such body corporate holds not less than one-fourth of the equity shares in the other or controls the composition of not less than one-fourth of the total membership of the Board of directors of the other; or
- (iv) if one or more directors of one such body corporate constitute, or at any time within a period of six months immediately preceding the day when the question arises as to whether such bodies corporate are under the same management, constituted (whether independently or together with relatives of such directors or employees of the first mentioned body corporate) one-fourth of the directors of the other; or
- (v) if the same individual or individuals belonging to a group, while holding (whether by themselves or together with their relatives) not less than one-fourth of the equity shares in one such body corporate also hold (whether by themselves or together with their relatives) not less than one-fourth of the equity shares in the other; or

- (vi) if the same body corporate or bodies corporate belonging to a group, holding, whether independently or along with its or their subsidiary or subsidiaries, not less than one-fourth of the equity shares in one body corporate, also hold not less than one-fourth of the equity shares in the other; or
- (vii) if not less than one-fourth of the total voting power in relation to each of the two bodies corporate is exercised or controlled by the same individual (whether independently or together with his relatives) or the same body corporate (whether independently or together with its subsidiaries); or
- (viii) if not less than one-fourth of the total voting power in relation to each of the two bodies corporate is exercised or controlled by the same individuals belonging to a group or by the same bodies corporate belonging to a group, or jointly by such individual or individuals and one or more of such bodies corporate; or
- (ix) if the directors of one such body corporate are accustomed to act in accordance with the directions or instructions of one or more of the directors of the other, or if the directors of both the bodies corporate are accustomed to act in accordance with the directions or instructions of an individual, whether belonging to a group or not.

Explanation II.— If a group exercises control over a body corporate, that body corporate and every other body corporate, which is a constituent of, or controlled by, the group shall be deemed to be under the same management.

Explanation III.— If two or more bodies corporate under the same management hold, in the aggregate, not less than one-fourth equity share capital in any other body corporate, such other body corporate shall be deemed to be under the same management as the first mentioned bodies corporate.

Explanation IV.— In determining whether or not two or more bodies corporate are under the same management, the shares held by financial institutions in such bodies corporate shall not be taken into account.

Illustration

Undertaking B is inter-connected with undertaking A and undertaking C is interconnected with undertaking B. Undertaking C is inter-connected with undertaking A; if undertaking D is inter-connected with undertaking C, undertaking D will be inter-connected with undertaking B and consequently with undertaking A; and so on.

Explanation V. - For the purposes of this clause, "group" means a group of two or more individuals, associations of individuals, firms, trusts, trustees or bodies corporate (excluding financial institutions), or any combination thereof, which exercises, or is established to be in a position to exercise, control, directly or indirectly, over anybody corporate, firm or trust; or associated persons.

Explanation VI. - For the purposes of this clause,

- (l) a group of persons who are able, directly or indirectly, to control the policy of a body corporate, firm or trust, without having a controlling interest in that body corporate, firm or trust, shall also be deemed to be in a position to exercise control over it;

- (II) "associated persons"—
- (a) in relation to a director of a body corporate, means—
 - (i) a relative of such director, and includes a firm in which such director or his relative is a partner;
 - (ii) any trust of which any such director or his relative is a trustee;
 - (iii) any company of which such director, whether independently or together with his relatives, constitutes one-fourth of its Board of directors;
 - (iv) any other body corporate, at any general meeting of which not less than one-fourth of the total number of directors of such other body corporate are appointed or controlled by the director of the first mentioned body corporate or his relative, whether acting singly or jointly;
 - (b) in relation to the partner of a firm, means a relative of such partner and includes any other partner of such firm; and
 - (c) in relation to the trustee of a trust, means any other trustee of such trust;
- (III) where any person is an associated person in relation to another, the latter shall also be deemed to be an associated person in relation to the former;
- (ii) "**relative**" shall have the meaning assigned to it in Clause (41) of Section 2 of the Companies Act, 1956 (1 of 1956);
- (c) "**place of removal**" means:
- (i) a factory or any other place or premises of production or manufacture of the excisable goods;
 - (ii) a warehouse or any other place or premises wherein the excisable goods have been permitted to be deposited without payment of duty or from where such goods are removed;
 - (iii) a depot, premises of a consignment agent or any other place or premises from where the excisable goods are to be sold after their clearance from the factory.
- (cc) "**time of removal**", in respect of the excisable goods removal from the place of removal referred to in Sub-Clause (iii) of Clause (c) shall be deemed to be the time at which such goods are cleared from the factory.

Transaction Value means the price actually paid or payable for the goods when sold and includes in addition to the amount charged as price any amount that the buyer is liable to pay to or on behalf of the assessee by reason of or in connection with the sale whether payable at the time of the sale or at any other time including but not limited to any amount charged for or to make provision for advertising or publicity marketing and selling organization expenses storage outward handling servicing warranty commission or any other matter; but does not include the amount of duty of excise sales tax and other taxes, if any, actually paid or actually payable on such goods.

Valuation of goods under Section 4 is made when –

- *Specific rates of duty are not applicable, i.e. where ad valorem basis is to be adopted;*
- *Tariff values are not notified for the goods under Section 3(2)*
- *The excisable goods are not notified for valuation under Section 4A.*

Under the new Section 4, effective from 1-7-2000, assessment of excisable goods is made on the basis of transaction value (T.V.). "Transaction value" means sales value, i.e., the total consideration in the transaction of sale. Under the new section, the invoice price is the basis for valuation. Each transaction of sale is valued separately on the basis of its sales value.

Section 4(1) reads as follows: Where the duty of excise is chargeable on any excisable goods with reference to their value, then, on each removal of the goods, such value shall–

- (a) In a case where the goods are sold by the assessee, for delivery at the time and place of the removal, the assessee and the buyer of the goods are not related and the price is the sole consideration for the sale, be the transaction value.
- (b) In any other case, including the case where the goods are not sold, be the value determined in such manner as may be prescribed.

In other words, when duty is charged on value of goods sold, its Transaction Value (adjusted sales value) is the assessable value of such sale. Each removal of goods is distinct and has a Transaction Value of its own i.e. different removals may have different Transaction Value.

For Transaction Value to be accepted as the assessable value following three conditions must be satisfied:

1. *The goods are sold by the assessee for delivery at the time and place of removal;*
2. *The assessee and the buyer are not related; and*
3. *The price is the sole consideration for the sale.*

If any of these three conditions are not fulfilled, Transaction Value is not accepted and valuation rules apply in such cases.

Hence, the transaction value cannot be applied in the following cases:

- When there is no sale;
- There is sale, but it is made to a related person or sale and delivery are not from the place of removal.
- Consideration in such sale is not the sole consideration.

1. Time and place of removal:

Goods sold at the time and place of removal means:

- (i) there is sale at the time of removal; and

- (ii) such sale is for delivery at the place of removal i.e. place of removal and place of delivery are same. Obviously, the price is ex-factory price and ownership is changing hands at the place of removal itself.

The place of removal has been defined under Section 4(3)(c) as, (i) "factory or any other place or premises of production or manufacture of the excisable goods; (ii) a warehouse or any other place or premises wherein the excisable goods have been permitted to be deposited without payment of duty, from where such goods are removed."

- (iii) Sales depot, or any such place where goods are sold from after removal from factory.

Assessee has been defined as a person who is liable to pay duty under the Act and includes his agent. [Section 4(3)(a)].

Note. Sales depot, place of consignment agent, branch office etc. are brought within the purview of the place of removal under the new definition but the sale from them is governed by Rule 7 of Valuation Rules.

In conclusion, the first condition is satisfied when:

- *there is sale at the time of removal;*
- *the delivery is from factory / warehouse;*
- *such delivery is for the purpose of sale from the factory or warehouse.*

2. Assessee and Buyer are not related:

Even if there is sale, the transaction value on such sale is not acceptable if the assessee (manufacturer) and the buyer are related: Section 4 (3) clarifies that persons shall be deemed to be related if-

- they are inter-connected undertakings;
- they are relatives;
- amongst them the buyer is a relative and distributor of the assessee, or a sub-distributor of such distributor; or
- they are so associated that they have interest, directly or indirectly in the business of each other.

"Inter-connected undertaking" has been defined under Section 2(g) of MRTP Act and the term "relative" is defined under the Companies Act, 1956.

The definition is more clarificatory than the one under the old Section 4 whether the assessee and buyer are related is a question of fact. However, under the last category of mutuality of interest, there are lots of recorded case laws which are relevant even under the new section.

In ***Cyril Laboratories v. CCE, Hyderabad***, it was held that mere sharing of common premises and establishment expenses doesn't mean that there is mutuality of interest as there is no financial interest in each others activity.

Similarly, in ***Food Specialties Case***, the Supreme Court held that financial arrangements and decision making process should commonly exist and mere share holding by the brand in any case where it is found that the assessee and the buyer

are related, transaction value can not be applied. The value in such a case is decided as per the Rules 9/10 of the Valuation Rules.

In ***Alembic Glass Industries v. CCE 2002 (SC)*** Two limited companies having common shareholding and common directors does not necessarily mean the companies are mutually interested in the business of each other.

3. Price is the sole consideration

The price paid by the buyer need not necessarily be the sole consideration. There may be some other considerations in addition to the price. If there is any other consideration that could possibly influence price, the assessable value has to be determined under Rule 6.

When there is a sale from the factory/ warehouse at the time of removal of goods and such sale is made for full commercial consideration to an unrelated person, such sales value is accepted as transaction value. Otherwise, valuation is made according to Valuation Rules, 2000.

Ingredients of transaction value are:

- It is the price actually paid or payable for the sale of goods.
- It is the price realized on sale.
- It includes any amount the buyer is liable to pay.
- It includes any amount liable to be paid on behalf of the assessee.
- The amount should be by reason of or in connection with the sale.
- It may be payable at the time of sale or any other time.
- It includes but is not limited to any amount charged for advertising, marketing, publicity, storage etc.
- It doesn't include the duty of excise, sales tax and other taxes.
- The transaction value is of wider import. It includes many things which were agitated earlier before the courts under the old provisions of valuation.
- The transaction value doesn't even have the mention of certain terms like packing expenses, discounts and so on. Yet, it can be interpreted that the transaction value is the net realizable sale price, after deducting all the discounts under normal trade practice.
- The packing expenses if any, are automatically included in the transaction value. Only the durable, returnable packing expenses charged from the buyer may be eligible for deduction.
- The concepts, such as post manufacturing expenses, post removal expenses propounded in *Bombay Tyres International and MRF Ltd.* cases respectively, have no direct bearing on the definition of transaction value. This definition is wide enough to include even post-removal expenses. Eg. after sales service charges collected from the buyer.

Deductions: Only excise duty and sales tax have direct mention as deductions, though of course, interest on delayed payments is not part of the transaction value.

Discounts allowed in the normal trade needs no special mention as the concept of Transaction Value is the net amount that is payable by the buyer after all such deductions.

- The terms such as liable to pay 'by reason of, or in connection with sale' are not defined. They may necessitate judicial interpretation. The definition has given ample scope to the department to claim variety of items to be included in the transaction value which the assessee may find difficult to cope with.
- The definition lays emphasis on what is payable by the buyer for the purchase of goods. The nature of such payments, whether it relates to manufacturing, selling, post manufacturing, post selling etc. is irrelevant now. The amount is includible if it is by reason of or in connection with sale.
- It may be noted that any amount spent by the buyer on his own account (eg. Advt.) and not payable to the seller because of sale, is not includible in the assessable value. In *LML Ltd. v. CCE*, 2001 (129) ELT, the Tribunal held that in case of common share of advertisement expenses, only seller's share of advertisements is includible in assessable value.
- Regarding the notional interest on advances paid by the buyer, the Supreme Court held in Metal Box case that notional interest is to be added to the price when there is nexus between sale and such advance i.e. when the advance influences the price.
- Conversely, in *VST Industries v. CCE*, 1998, the Supreme Court held that if the price charged from all the customers is same though some customers have advance deposits with the company, the notional interest need not be loaded into the price as the advances have no influence on price.

Valuation Rules: The valuation of excisable goods is made with the help of Rules when transaction value cannot be applied directly. Section 4(1)(b) specifies that rules have to be resorted to, where there is no sale or where the conditions under Section 4(1)(a) are not satisfied.

Rule 4. When there is no sale at the time of removal: When there is no sale at the time of removal, sale price is not available. Naturally, transaction value is not available. Then, the following methodology is prescribed under Rule 4.

- Take the price of such goods sold at the time nearest to the time of removal.
- Make reasonable adjustments. These adjustments may be with reference to any price fluctuations during the time lag between these two removals, difference in the quality, and packing material used and so on.

This rule is not applied in case of stock consumption and captive transfer, even though, there is no sale in those two situations. For them there are separate rules i.e. Rules 7 and 8 respectively.

It may be noted that in a recent circular issued by the Board, it was specified that for gifts and free samples, Rule 4 is applicable.

If an item falling under Section 4A is distributed as a free sample without printing of MRP such goods are to be valued under Rule 4, i.e. at the price of the nearest time of removal vide Circular No. 813/10/2005 CX dated 25.4.2005.

Rule 5: Delivery for sale not at the place of removal: Rule 5 is applicable when there is a sale at the time of removal, but delivery is not at factory, but at some

other place, say, the place of buyers. This is a situation where F.O.R. [free on road/rail] price is quoted in the invoice. Since the price is not ex-factory price, transaction value cannot be applied. Hence, valuation is done under Rule 5.

Conditions necessary for the application of Rule 5:

- Place of removal and place of delivery are not same.
- Price quoted is F.O.R. price, including the cost of transportation and insurance from the factory to the place of buyer. [F.O.R. - free on road]
- The price for the purpose of valuation will be the price charged from the buyer i.e. F.O.R. price – the cost of transport up to the point of delivery. (F.O.R. price - cost of transport etc.)
- If the manufacturer uses his own vehicles freight charges as certified by a CA / CWA are allowed to be deducted from F.O.R. price.
- Equalised freight charges are allowed to be deducted from F.O.R value.

Equalised freight: This is an average of the freight charges allowed to be deducted uniformly for all sales to different destination. This is possible only when the sale is from factory.

Illustration:

A manufacturer has factory at Hyderabad. He has uniform price of ₹ 1,000 (excluding taxes) per unit for sale all over India. Sale is made from Hyderabad.

During 2011-2012 he made the following sales:

<i>Place of delivery</i>	<i>No. of units</i>	<i>Transportation Charges</i>
Hyderabad	1000	Nil
Chennai	500	15,000
Delhi	700	50,000
Ahmedabad	<u>800</u>	<u>25,000</u>
Total	<u>3,000</u>	<u>90,000</u>

What is the assessable value?

$$\text{Average charges per unit} = \frac{90,000}{3,000} = ₹ 30/-$$

$$\therefore \text{Assessable value per unit} = (1,000 - 30) = ₹ 970/-$$

Rule 6 – Price not sole consideration: Apply this rule under the following conditions:

- There is a sale at the place of removal, but the consideration received is not the total consideration. It means, if the same goods are sold in the open market, they would fetch more money.
- Aggregate consideration is arrived at by adding all other considerations to the transaction value, that flowed directly or indirectly from the buyer to the assessee.

- The value of the items given are added to the consideration to make it the transaction value i.e.
- Value of materials, components, parts and similar items relatable to such goods.
- Value of tools, dies, moulds, drawings, blue prints, technical maps and charts and similar items used in the production of such goods.
- Value of material consumed, including packaging materials in the production of such goods.
- Value of engineering, development, art work, design work and plans and sketches.
- Interest on advance amount received from the buyer is added to the transaction value. In Metal Box Ltd., Ponds India advanced huge amount to Metal Box company and enjoyed 50% bulk discount on its purchases. HELD: Discount may be allowed when the interest is added to the sale price to arrive at the assessable value.
- Cenvat credit availed on the inputs should be deducted from the cost of such inputs. [*Dai Ichi Karkaria Ltd.* 1999, S.C.]

The value of above items is added to the extent they are not included in the transaction value even if they are received indirectly, or received free of cost. Earlier, in Hindustan Polymers case, the Supreme Court held that the packing material supplied by buyer is not includible in the assessable value. But as per the present scheme of valuation under Rule 6, it is includible.

Rule 7 – When goods are sold from sales depot, or any other place: When there is removal of goods from factory as stock transfer, to the sales depot, place of consignment agent or any other place, the value of the goods will be the price prevailing at the depot, etc. on the date of removal from the factory.

As per the rules, assessment is to be made at the time of removal of goods from the factory or warehouse as the case may be. Dutiability and rate of duty are ascertained on the date of removal. As assessment is necessary on the date of removal, the price prevailing at the place of sale on the date of removal is taken.

- For instance, the goods are cleared from the factory today for sale to be made from the depot, the duty is assessed on the basis of the price prevailing at the depot today. It means it is the price at which actual transaction took place today at the depot.
- If there is no sale and the price is not available at the depot on the date of removal from the factory/ warehouse, then the price at the depot on the date (preceding) nearest to the date of removal shall be taken.
- If different quantities are sold at different rates, then the price of the aggregate quantity [greatest quantity] sold on that day or on the date nearest to the removal shall be taken. If the above scheme can not be applied then rule 11 shall be applied.

Rule 8 – When goods are not sold but captively consumed: Captive consumption means self consumption. When the goods manufactured are not sold but are reused in the factory for the manufacture of other articles, the value for the purpose of excise shall be 110% of the cost of production. Here, the valuation is based on the cost sheet certified by a Cost Accountant/Chartered Accountant.

In a land mark decision in *Dai Ichi Karkaria Ltd.*, S.C. 1999, the Supreme Court held that in arriving at the price on the basis of cost sheet for captive consumption, the CENVAT credit availed on raw material should be deducted from the cost of raw-material. The Apex court relied on the Guidance Note issued by the Institute of Chartered Accountants of India. The methodology of costing as suggested by the ICWAI in CAS-4 has been approved by CBEC.

Rule 9 - Sale to related person other than inter connected undertaking: This rule covers those situations where goods are sold to or through related persons other than the Inter-Connected undertakings. In such a case, the value shall be the normal transaction value at which these are sold by the related person at the time of removal to unrelated persons. Normal transaction value means price of the greatest aggregate quantity. If the related person further sells to his related person who is a retailer, then the price charged to the retailr (even though he is a related person) will be accepted for assessment. If the goods are not sold by the related person, but consumed captively, the value shall be determined as per Rule 8. i.e. 110% of cost of production.

Rule 10 – Sale to/through inter-connected undertakings (and related): If the inter-connected undertakings also happen to be the related persons under the remaining clauses or they happened to be holding and subsidiary companies, then Transaction Value shall be determined as per Rule 9. In any other case (i.e. the buyer and the seller are merely the inter-connected undertakings), the value shall be determined under Section 4(1)(a), as if they are not related persons at all.

Mere interconnection doesn't affect the valuation. If the Inter-connected Undertakings are otherwise related under other clauses, then only Rule 9 is applied.

Rule 10A – Valuation Under Job Work: According to this rule, where goods are manufactured by job worker on behalf of a person (commonly known as principal manufacturer), the value for payment of excise duty would be based on the sale value at which the principal manufacturer sells the goods, ***as against the earlier practice where the value is taken as cost of inputs plus the job charges.***

- The price charged by the principal manufacturer at the time of removal of goods from the premises of the job worker shall be taken for valuation.
- Such price shall be sole consideration and the principal manufacturer and the buyer shall not be related persons.
- If the price is not sole consideration, follow the mechanism given under Rule 6 and if the transaction is related persons transaction, follow Rule 9.

If the goods are removed at a place other than the place of job worker, then apply normal transaction value of that place of removal as is done under Rule 7.

With the advent of Rule 10A, the Valuation procedure specified by Supreme Court in Ujagar prints case became invalid.

Rule 11 – Residual method/method of reasonable means: When the value cannot be determined by any of the valuation rules, it shall be determined using reasonable means consistent with the principles and general provisions of these rules and Section 4(1).

THE CENTRAL EXCISE VALUATION (DETERMINATION OF PRICE OF EXCISABLE GOODS) RULES, 2000

Notification No. 45/2000 - Central Excise (N.T.)

Dated 30th June, 2000

G.S.R. (E) — In exercise of the powers conferred by Section 37 of the Central Excise Act, 1944 (1 of 1944) and in supersession of the Central Excise (Valuation) Rules, 1975 except as respect things done or omitted to be done before such supersession, the Central Government hereby makes the following rules, namely:

1. (1) These rules may be called the Central Excise Valuation (Determination of Price of Excisable Goods) Rules, 2000.
- (2) They shall come into force on and from the 1st day of July, 2000.

CHAPTER I Preliminary

2. In these rules, unless the context otherwise requires:
 - (a) “Act” means the Central Excise Act, 1944 (1 of 1944);
 - (b) “**normal transaction value**” means the transaction value at which the greatest aggregate quantity of goods are sold;
 - (c) “**value**” means the value referred to in Section 4 of the Act;
 - (d) words and expressions used in these rules and not defined but defined in the Act shall have the meanings respectively assigned to them in the Act.

CHAPTER II Determination of Value

3. The value of any excisable goods shall, for the purposes of Clause (b) of Sub-section (1) of Section 4 of the Act, be determined in accordance with these rules.
4. The value of the excisable goods shall be based on the value of such goods sold by the assessee for delivery at any other time nearest to the time of the removal of goods under assessment, subject, if necessary, to such adjustment on account of the difference in the dates of delivery of such goods and of the excisable goods under assessment, as may appear reasonable.
5. Where any excisable goods are sold in the circumstances specified in Clause (a) of Sub-section (1) of Section 4 of the Act except the circumstance in which the excisable goods are sold for delivery at a place

other than the place of removal, then the value of such excisable goods shall be deemed to be the transaction value, excluding the actual cost of transportation from the place of removal upto the place of delivery of such excisable goods provided the cost of transportation is charged to the buyer in addition to the price for the goods and shown separately in the invoice for such excisable goods.

6. Where the excisable goods are sold in the circumstances specified in Clause (a) of Sub-section (1) of Section 4 of the Act except the circumstance where the price is not the sole consideration for sale, the value of such goods shall be deemed to be the aggregate of such transaction value and the amount of money value of any additional consideration flowing directly or indirectly from the buyer to the assessee.

Explanation: For removal of doubts, it is hereby clarified that the value, apportioned as appropriate, of the following goods and services, whether supplied directly or indirectly by the buyer free of charge or at reduced cost for use in connection with the production and sale of such goods, to the extent that such value has not been included in the price actually paid or payable, shall be treated to be the amount of money value of additional consideration flowing directly or indirectly from the buyer to the assessee in relation to sale of the goods being valued and aggregated accordingly, namely:

- (i) value of materials, components, parts and similar items relatable to such goods;
 - (ii) value of tools, dies, moulds, drawings, blue prints, technical maps and charts and similar items used in the production of such goods;
 - (iii) value of material consumed, including packaging materials, in the production of such goods;
 - (iv) value of engineering, development, art work, design work and plans and sketches undertaken elsewhere than in the factory of production and necessary for the production of such goods.
7. Where the excisable goods are not sold by the assessee at the time and place of removal but are transferred to a depot, premises of a consignment agent or any other place or premises (hereinafter referred to as "such other place") from where the excisable goods are to be sold after their clearance from the place of removal and where the assessee and the buyer of the said goods are not related and the price is the sold consideration for the sale, the value shall be the normal transaction value of such goods sold from such other place at or about the same time and, where such goods are not sold at or about the same time, at the time nearest to the time of removal of goods under assessment.
 8. Where the excisable goods are not sold by the assessee but are used for consumption by him or on his behalf in the production or manufacture of other articles, the value shall be one hundred and ten per cent of the cost of production or manufacture of such goods.
 9. When the assessee so arranges that the excisable goods are not sold by an assessee except to or through a person who is related in the manner specified in either of sub-clause (ii), (iii) or (iv) of Clause (b) of Sub-section

(3) of Section 4 of the Act, the value of the goods shall be the normal transaction value at which these are sold by the related person at the time of removal, to buyers (not being related person); or where such goods are not sold to such buyers, to buyers (being related person), who sells such goods in retail :

Provided that in a case where the related person does not sell the goods but uses or consumes such goods in the production or manufacture of articles, the value shall be determined in the manner specified in Rule 8.

10. When the assessee so arranges that the excisable goods are not sold by him except to or through an inter-connected undertaking, the value of goods shall be determined in the following manner, namely:
- (a) If the undertakings are so connected that they are also related in terms of Sub-clause (ii) or (iii) or (iv) of Clause (b) of Sub-section (3) of Section 4 of the Act or the buyer is a holding company or subsidiary company of the assessee, then the value shall be determined in the manner prescribed in Rule 9.
- Explanation:* In this clause "holding company" and "subsidiary company" shall have the same meanings as in the Companies Act, 1956 (1 of 1956).
- (b) In any other case, the value shall be determined as if they are not related persons for the purpose of Sub-section (1) of Section 4.
11. If the value of any excisable goods cannot be determined under the foregoing rules, the value shall be determined using reasonable means consistent with the principles and general provisions of these rules and Sub-section (1) of Section 4 of the Act.

(T.R. Rustagi)

Joint Secretary to the Government of India

F.No. 354/81/2000-TRU

THE CENTRAL EXCISE (DETERMINATION OF RETAIL SALE PRICE OF EXCISABLE GOODS) RULES, 2008

Notification No. 13/2008 effective from 1st March, 2008

Rule 1	Short Title
Rule 2	Definitions
Rule 3	The retail price under Section 4A(4) shall be determined in accordance with these rules.
Rule 4	(a) Where a manufacturer removes the goods under Section 4A(1) without declaring the retail price; or (b) Declared price is not as per law; or (c) Obliterates the price after removal from place of manufacture.

	<p>Then the price is ascertained in the following manner:</p> <p>(i) take market price of identical goods removed by the manufacturer within a period of one month before or after removal of such goods.</p> <p>(ii) if the retail price can not be ascertained as above, it shall be ascertained by conducting market enquiries in the retail market.</p> <p>If more than one retail price is ascertained in the above cases, the highest of them shall be taken for assessment.</p>
Rule 5	<p>If the manufacturer alters or tampers the price after removal and it results in increase of retail price, then such increased price shall be taken as price for all goods removed one month before and after the removal of such offended goods.</p> <p>If the alteration or tempering results in increase of more than one price, the highest of them shall be taken.</p>
Rule 6	<p>If the price cannot be ascertained under the above rules [Rules 4 & 5], it shall be ascertained as per the provisions under Section 4A and the above rules.</p>

6.5 Payment of Excise Duties

1. Basic Provisions in Law

While duty liability is, no doubt, created by the act of manufacture, still, it should be impractical or unviable for the manufacturer to discharge the liability immediately, that is, at the very moment when the goods, are manufactured. Hence, the excise law has provided for postponement of payment of duty to a latter point of time. In *Bombay Tyre International's case* [1983 ELT 1896 (SC)], the Supreme Court upheld the Legislature's choice of convenience in collecting the levy at the time of clearance of the excisable goods. Rule 4 and Rule 8 of Central Excise Rules, 2002 read together would indicate that duty has to be paid only at the time when the goods are removed from the premises of manufacturer or any other specified places.

2. The Rate of Duty to be charged on Goods

Section 3 of the Central Excise Act, 1944, which creates the charge and defines the nature of the charge of this tax, provides that the duties shall be paid at the rates set forth in the Schedules to the Central Excise Tariff Act, 1985. The rates at which excise duty is charged are thus prescribed in the Tariff Act which contains elaborate classification of goods and rate structure of duties. However, these rates are liable to be changed from time to time. Further, while the levy is on the manufacture or production of goods, the stage of collection need not, at a point of time, synchronise with the completion of the manufacturing. These principles are in fact, embodied in the Central Excise Law in as much as Section 3 of the Act stipulates 'manufacture' as the taxable event, Rule 4 of the Central Excise Rules, on the other hand, stipulates 'removal of goods from the factory' or any other specified places as the point of time for collection of duty. The question therefore arises as to what rate of duty will be charged, if goods manufactured on one date are removed on a later date and in the meantime, the rate of duty applicable to the goods in question undergoes an upward revision or if the goods in question were not liable to duty when they were manufactured but on the date of removal they became liable to duty? In such a

situation, while Rule 5(1) of the Central Excise Rules provide that the rate of duty and tariff valuation applicable to any excisable goods other than khandsari molasses shall be the rate and value in force on the date of removal of goods from the factory or warehouse, as the case may be, the contention of the manufacturer, invariably would be that the manufacture being the taxable event, the rates prevailing on the date of manufacture should be levied.

The rate of duty in the case of **Khandsari molasses**, shall be the rate in force on the date of receipt of such molasses in the factory of the procurer of such molasses. It has also been provided in the Explanation to Rule 5(2) that if any excisable goods are used within the factory, the date of removal of such goods shall mean the date on which the goods are issued for such use.

As per Sub-rule (3) of this Rule, rate of duty in the case of goods falling under Chapter 62 of the First Schedule to the Central Excise Tariff Act 1985, produced or manufactured on job work, shall be the rate in force on the date of removal of such goods by the person getting the goods manufactured under the aforesaid Chapter.

Payment of Duty (Rule 8)

Rule 8 of the Central Excise Rules, 2002 lays the provisions relating to manner of payment of duty. Goods are cleared from the factory under an invoice and the duty is paid either by cash and/or CENVAT Credit. Liability for payment of duty on goods removed is immediate. But the Government allows the assessee to make the payment in monthly instalments.

In case of non-SSI assessee, for all the removals in a month, the duty can be paid by 5th of the following month or by 6th of the following month in case of e-payment.

In case of an SSI it is payable by 5th (6th in case e-payment) of the month following the particular quarter

In case goods removed in the month March, it is payable by 31st March. In case of SSI for the last Quarter starting on 1st January and ending on 31st March the duty is payable on 31st March.

- Payment is said to be made when the amount is credited to the account of the Central Govt.
- When the payment is made by a cheque, it is deemed to have been paid on the date of deposit of cheque subject to realization of it.
- Any amount due will be recovered as per the provisions of Section 11.
- Any amount due will be recovered with interest as per Section 11AB, from the due date.

Discontinuation of instalment facility: If the assessee is not able to pay duty and the default continues beyond 30 days, the instalment payment will be discontinued.

Consequently, the payment is to be made through bank or by PLA for each removal and cenvat credit cannot be utilized.

An Assessee, who has paid total duty of ₹ 10 lakh or more including the amount of duty paid by utilization of CENVAT credit in the preceding financial year shall

deposit the duty electronically through internet banking. [Rule 8(1) of Central Excise Rules, 2002]

Any payment made under Cenvat Credit Rules is duty for the purpose of this rule 8 and such payment can be made along with the payment made under this rule:

Payment of duty vis-à-vis taxable Event

The taxable event in regard to excise duties is therefore manufacture or production. While the duty no doubt is on the goods as such, it is the person who is responsible for the excisability being created, that is, the person who has brought forth the taxable event (which is the manufacture), who has to discharge the duty liability created by him.

While the goods acquire excisability by being manufactured, the excisability is extinguished by the duty therein being paid. The goods remain 'excisable goods' from the point of time when they are manufactured/produced, till the point of time when the duty is paid. Once duty is paid, the excisability is erased, and the goods will no longer be 'excisable goods'. They have to be termed as 'excised' or 'duty paid' goods.

Once it is understood that excisability created by manufacture can be extinguished only by payment of duty, the need naturally arises to exercise departmental control over the period when the excisability lasts. Otherwise, there could be a risk of goods being removed without payment of duty, that is, without the excisability being extinguished. The Central Excise Law contains elaborate provisions to ensure this aspect, and detailed procedures have also been evolved for fulfilment of this purpose. At the same time, the law and procedures take every possible care to ensure that the constraints placed upon the manufacturer for this purpose do not in any manner interfere unduly with the normal and natural pursuits of industry and trade.

6.6 CLEARANCE AND REMOVAL PROCEDURES

The Deptt. ensures duty payment before removal of excisable goods by prescribing the procedure for removal of such goods.

W.e.f. July 1, 2001, the existing Central Excise Rules, 1944 were substituted by New Central Excise (No. 2) Rules, 2002 which are again substituted by Central Excise Rules 2002. Prior to the introduction of these rules, the following procedures/methods were in operation for the purpose of removal of goods:

- (a) Self Removal Procedure (SRP);*
- (b) Physical Control;*
- (c) Compounded Levy Scheme.*

6.6.1 Self Assessment Method

All excisable goods are covered by self removal procedure, except cigarettes falling under Chapter 24 of the Central Excise Tariff, it has however not always been so. If we trace the evolution of excise in India, we would note that physical control was the method applicable to almost all excisable goods (with a few covered by Compounded Levy Scheme) upto the year 1968. This method as would be

elaborated later, requires rigid departmental control over the activities of the manufacturer, requiring presence of departmental authority for removal of every consignment from the factory. This inevitably created considerable hardship to the manufacturers functioning as an impediment to normal activities of manufacture and free flow of goods into the market. With rapid industrialisation, paralleled by progressive expansion of excise, the department also found it increasingly difficult to provide manpower to operate physical control in regard to the ever-increasing number of industrial units. These factors together prompted the introduction of a new system, the S.R.P. in 1968. It was a selective experiment confined to a few commodities to start with, but its scope was rapidly expanded to cover most of the excisable goods very soon. Since then not only gradually almost all the excisable goods have been brought under the cover of SRP but lots of procedural relaxations had been made under SRP Scheme paving way for payment of duty by the assessee on self-assessment basis.

Now, there is no distinction between 'physical control' and 'Self-Removal Procedure (SRP)'. **All goods are covered under SRP. The only exception is that in case of cigarettes, duty has to be assessed and the invoice is required to be countersigned by Excise Officer, rest of the procedures and rules are all common.**

The law relating to self assessment of duty is laid under Rule 6 of these Rules. Rule 6 of the Central Excise Rules, 2002 states that the assessee shall himself assess the duty payable on any excisable goods, provided that in case of cigarettes, the Superintendent or Inspector of Central Excise shall assess the duty payable before removal by the assessee.

The assessee is required to submit monthly return in ER-1 (earlier RT-12) Form. This return has to be filed along with "Self Assessment Memorandum" whereby, the assessee details that the particulars contained in ER-1 return are correctly stated, duty has been correctly assessed and paid as per the provisions of this Act. The return made shall be subject to scrutiny by the Departmental Officers, who may carry out surprise checks alongwith routine audit procedures.

6.6.2 Removal of goods on invoice

The provisions relating to removal of goods on an invoice are contained under Rule 11 of these Rules. It has been provided under Rule 4 of the Central Excise Rules, 2002 that excisable goods can be removed from the place of their manufacture/production only on payment of duty, unless otherwise provided. Rule 8 lays down the provisions allowing payment of duty on fortnightly basis (monthly in case of SSI) thereby allowing clearance of goods from the factory without payment of duty.

Sub-rule (1) of Rule 11 provides that no excisable goods shall be removed from a factory or a warehouse except under an invoice signed by the owner of the factory or his authorised agent and in case of cigarettes each such invoice is required to be countersigned by the Inspector of Central Excise or the Superintendent of Central Excise before the Cigarettes are removed from the factory.

Invoice should be serially numbered and contain the registration number, description, classification, time and date of removal, rate of duty, quantity and value

of goods alongwith duty payable, mode of transport and registration number of vehicle thereon [Sub-rule (2)] under sub-rule (2) a proviso has been inserted vide Notification 7/2008 as follows: provided that in case of proprietor concern business owned by Hindu undivided family, the name of proprietor or HUF, as the case may be, shall also be mentioned in the invoice.

Rule 11(3) provides that invoice shall be prepared in triplicate and is required to be marked as under:

- (i) Original copy being marked as Original for Buyer;*
- (ii) Duplicate copy being marked as Duplicate for Transporter;*
- (iii) Triplicate copy being marked as Triplicate for Assessee.*

At a time, only one copy of invoice book shall be in use unless otherwise allowed by Assistant/Deputy Commissioner, as the case may be, in the special facts and circumstances of each case [Sub-rule (4)].

Each foil of the invoice book should be authenticated by the owner/working partner/managing director/Company Secretary, and also the serial numbers of the same should be intimated to the Superintendent of Central Excise having jurisdiction before being brought into use.

- **Contents:** the invoice shall contain
 - (i) description of goods;
 - (ii) quantity of goods;
 - (iii) value of goods;
 - (iv) amount of duty if any;
 - (v) E.C.C. No. of the assessee.
 - (vi) Vehicle with registration No. of the vehicle,
 - (vii) Address of the jurisdictional division office.
- Serial No. of the invoice book must be intimated to the ₹ Before use computerized invoices are also allowed but they should contain serial Nos. which are producible automatically.
- This invoice is an important document which must be made available for dept's examination, inspection as and when required.
- Cancellation of invoice must be intimated to the RS within 24hours. And the original must be sent to the Department.

6.6.3 Compounded Levy Scheme

Compounding of levies implies the assessee being authorised to pay a pre-determined sum to the department, at fixed periodical intervals, instead of paying duty on a consignment-to-consignment basis. The amount of duty to be paid is pre-determined by the department on the basis of various parameters pertaining to production. The advantage of compounding is that the assessee is freed from the procedural formalities being fulfilled by him for each consignment. The advantage to the department is that it reduces the need to control various factors pertaining to production and removal. The option has been made available in case of

manufacturers in unorganised sectors where accounting records are not adequate or proper for consumption and collection of duty payable on goods manufactured.

However, the system has been very selectively resorted to and apply only to a few items. Currently the scheme is applicable only to stainless steel patties/pattas and aluminum circles". The compounded levy scheme has been recently extended to panmasala and gutkha vide Notification No. 38/2007.

The procedure is that the assessee eligible to work under the scheme will first file an application for special procedure (ASP) before the Assistant Commissioner. The Assistant Commissioner will have the necessary investigations made to verify the eligibility as well as the amount to be paid by the assessee. The duty compounded, as prescribed in the schedule current at the time, will have to be paid by the assessee in the form prescribed therefor. The assessee is thus freed from almost all fetters such as maintaining separate accounts and submitting returns etc.

6.7 Remission of Duty (Rule 21)

Section 5 of the Central Excise Act, 1994, empowers the Central Govt. to make rules providing for remission of duty on loss of quantity due to natural causes.

Remission means cancellation or waiver of duty.

The manufacturer has to make an application to the appropriate authority for remission of duty for the loss of goods in the store room. The remission may be granted by various authorities depending upon the amount involved.

Grounds : goods lost or destroyed by

- natural causes
- unavoidable accident or
- goods are unfit for consumption or marketing

<i>Amount of Remission Rupees</i>	<i>Appropriate Authority</i>
Upto 10,000	Superintendent
Above 10,000 upto 1,00,000	Assistant Commissioner/Deputy Commissioner
Above 1,00,000 upto 5,00,000	Joint/Additional Commissioner
Above 5,00,000	Commissioner

6.8 ASSESSMENT

Assessment is quantification of the duty liability to be discharged by the assessee. Rule 2(b) of the Central Excise Rules, 2002 defines 'assessment' to include — self-assessment of duty made by the assessee and provisional assessment under Rule 7.

Accordingly assessment includes—

1. Self Assessment made by the Assessee,
2. Provisional Assessment under Rule 7.

1. Self-assessment

Under the self-assessment system introduced in 1996 for removals under Self Removal Procedure (SRP), the assessee is himself allowed to assess the duty liability and prepare a return on a monthly-basis (for SSI on quarterly-basis) and submit to the Central Excise Department. The Departmental officers are required to scrutinise the returns in the manner prescribed.

2. Provisional Assessment

Where the assessee is not in a position to determine either the value of the goods or the applicable rates of duty, in such circumstances, the remedy available to the assessee and the officer is the "Provisional Assessment". The provisional assessment is thus a temporarily arrangement to keep the machinery in motion. The duty is thus assessed based on the available information and the goods are cleared after its payment. The final assessment is made on removal of reasons which necessitated the provisional assessment.

The provisions relating to the provisional assessment are laid under Rule 7 of the Central Excise Rules, 2002. Provisional Assessment can be requested by an assessee and department cannot order provisional assessment.

Provisional assessment can be resorted to by an assessee under Rule 7(1) where he is unable to determine the value of excisable goods or rate of duty applicable thereto. In the aforesaid cases, assessee may request Assistant/Deputy Commissioner in writing giving reasons for payment of duty on provisional basis. After such request the Assistant/Deputy Commissioner may by order allow payment of duty on provisional basis and may also specify the rate or value at which the duty shall be paid on provisional basis.

As per the provisions of Rule 7(2), the Assistant/Deputy Commissioner may allow an assessee to make payment of duty on provisional basis if he executes a bond in prescribed form with such surety or security in such amount as the Assistant/Deputy Commissioner of Central Excise deem fit, binding the assessee for payment of difference between the amount of duty as may be finally assessed and the amount of duty provisionally assessed.

The Assistant/Deputy Commissioner shall pass order for final assessment under Rule 7(3) after getting relevant information within six months of date of communication of his order allowing provisional assessment. This period of six months can be extended by the Commissioner of Central Excise, on sufficient cause being shown and the reasons to be recorded in writing for a further period not exceeding six months and by the Chief Commissioner of Central Excise for such further period as he may deem fit.

In case of provisional assessment, final assessment will be done by Assistant/Deputy Commissioner. After final assessment if the duty payable is more the difference will be paid by assessee. In case, the duty finally assessed is less; difference will be refunded [(Rules 7(4) and 7(5)]. Where the differential duty is found to be payable, interest at the rate specified by the Central Government by notification issued under Section 11AB of the Act shall be payable by the assessee from first day of month succeeding the month for which such amount is determined till date of

payment thereof. Thus, interest is payable only after assessment is finalised by Assistant/Deputy Commissioner of Central Excise.

In case differential amount is required to be refunded to the assessee, it shall be refunded with interest at the rate specified by the Central Government by notification issued under Section 11 BB of the Act from first day of the month succeeding the month for which refund is determined till the date of refund.

Sub-rule (6) of Rule 7 lays that refund is subject to the provisions of "Unjust Enrichment" i.e. refund will be granted to manufacturer if he has not passed on incidence of duty to another person. As per this sub-rule, any amount of refund determined under Sub-rule (3) shall be credited to the Consumer Welfare Fund. However, it has been provided that the amount of refund, instead of being credited to the fund, be paid to the applicant, if such amount is relatable to:

- (a) the duty of excise paid by the manufacturer, if he had not passed on the incidence of such duty to any other person, or
- (b) the duty of excise borne by the buyer, if he had not passed on the incidence of such duty to any other person.

6.9 Filing of return

Rule 12 of the Central Excise Rules, 2002 lays down the provisions relating to filing of return. As per Sub-rule (1) of this Rule, every assessee is required to submit a monthly return in proper form of production or removal of goods and other relevant particulars to the superintendent of Central Excise, within ten days after the close of the month to which the return relates.

It has also been provided that where an assessee is availing the exemption under a notification based on the value of clearances in a financial year, he shall file a quarterly return in proper form of production and removal of goods and other relevant particulars within twenty days after the close of the quarter to which the return relates. According to Notification, the return is required to be filed in quintuplicate in Form ER-1 (EOU/EPZ/SEZ units are required to file return in Form ER-2). For SSIs Form ER-3 has been prescribed.

If there is delay in payment of duty, interest should also be deposited before filing ER-1 return. This return is acknowledged by Superintendent of Central Excise and one copy duly acknowledged is returned to the assessee.

Electronic Filing (E-filing of return)

Where an assessee has paid total duty of ₹10 lakh or more including the amount of duty paid by utilization of CENVAT credit in the preceding financial year, he shall file monthly/quarterly return, electronically.

Return shall be accompanied by treasury receipts challans for deposit of duty, original and duplicate copies of PLA and extracts of CENVAT register and other documents as required by the commissioner.

6.10 Large Tax Payer Units

Concept: It is a self contained tax administration office under the department of revenue acting as a single window clearance point for all matters relating to Central Excise, Income Tax/Corporate Tax and Service Tax. Chief Commissioner of

Excise/Income tax will be the incharge of the unit. These have been established initially in the major cities in India. Bangalore Chennai and units are already in function. Large taxpayer means a person who has one or more registered premises under the Central Excise or service tax law, who is an assessee under Income Tax who holds PAN and being a manufacturer of excisable goods or provider of taxable services has paid

- ₹ 5 crore or more in cash or through current account as excise duty
- ₹ 5 crore or more in cash or through current account as service tax
- ₹ 10 crore or more in cash as advance tax under Income Tax Act

during the financial year preceding the year in which application is made.

However, manufacturers of cigarettes and pan masala are not eligible under this scheme.

Filing of returns: All returns relating to Direct Taxes, Excise and Service Tax can be files at one place irrespective of geographical location of their units.

Filing of other documents: other documents, intimations, proofs, bonds etc. can be filed with LTUs.

Lesser interaction with the departmental officers: An officer of the rank of A.C. and above will be appointed as client executive to deal with the matters of each tax payer. All issues can be taken up with him for guidance, procedural aspects and so on.

Disputes: All legal disputes pending at department level including demand notices will be transferred to LTU.

Procedural relaxations: The tax payers availing this scheme also enjoy certain procedural relaxations. Following are from Central Excise:

Under CENVAT Credit Scheme (Rule 12A): The large tax payer unit is allowed to transfer inputs or capital goods from one unit to another unit under cover of transfer challan or invoice:

1. The transferee unit should use the inputs for manufacture of final products and clear the goods by payment of duty within a period of 6 months from the date of receipt of inputs.
2. Alternatively the transferee unit can also export final products without payment of duty within six months.

6.11 EXCISE DUTY — EXEMPTIONS

6.11.1 Introduction

To recapitulate, democracy, as even the word etymologically indicates, is the power of the people. The rulers rule, because the people have authorised them to rule. While every power exercised by a democratic government must have the sanction of the people, the important power of taxation is also subject to the same principle that it should be authorised by the people. This concept is enshrined in

Article 265 of our Constitution which states “no tax shall be levied or collected except by authority of law”.

In pursuance of the principle and constitutional prescription as examined above, Union Excise Duties are levied by virtue of the power conferred upon the Government by the Union Legislature through the Central Excise Act, 1944 (hereinafter referred to as the ‘Act’). Section 3 of the Act explicitly states that duties of excise on goods produced or manufactured in India shall be levied at the rates specified in the First Schedule and the Second Schedule to the Central Excise Tariff Act, 1985.

The rates prescribed in the Central Excise Tariff are termed as ‘statutory rates’ since these are the rates prescribed in the statute. Often times, they are also referred to as ‘standard rates’ or ‘tariff rates’.

6.11.2 Problems faced in administration of indirect taxes

While the legislature alone has the power to prescribe rates of taxation, indirect taxes like Excise and Customs, however, pose a problem which makes it almost impossible to observe this principle to the hilt. The tax base for indirect taxes is the entire field of manufacturing industry and trade. Once this is noted, the fact which immediately should strike one is that it is not a static field, but a field which exhibits ebullient dynamism. In this field, most factors change frequently and fast. New products, new processes, new marketing methods etc. are constantly thrown up. To suit the ever changing needs and match the features of a dynamic tax base like industry and trade, the fiscal administration should also be equipped with the ability to vary the rates whenever emergent situations warrant such variations.

Thus, while flexibility should be a very important feature of tax rates in commodity taxation, the basic principle of legislative mandate for each change of rate of duty would militate considerably against it.

While the legislature can no doubt change the rates of duty prescribed by it (statutory rates), still it is common knowledge that the legislative process itself is quite elaborate and time consuming. Hence, while on the one hand, rates of duty have to be altered with utmost despatch, on the other, it may not be possible to have it done through the legislative process. The solution to the problem is through the instrument of duty exemptions.

6.11.3 The concept of exemptions

Flexibility in the matter of rates of duty of excise is brought through the power vested in the executive arm of the Government by the legislature itself, to reduce the rates of duty from what the statutory rates is. Section 5A of the Central Excise Act, 1944, confers this power on the Government.

Provisions of Section 5A

Section 5A(1) of the Central Excise Act, 1944 empowers the Central Government to exempt any excisable goods either from the whole of duty prescribed (the statutory rate) or a part thereof. The former is commonly known as total exemption while the latter is referred to as partial exemption. Each such an

exemption should be announced through a Notification in the Gazette of India. The exemption may be a 'straight exemption', that is, without any condition attached to it, or it may be a 'conditional exemption' to which only assessee fulfilling the conditions specified are eligible. Sub-section (1A) lays that where an exemption under Sub-section (1) in respect of any excisable goods from the whole of the duty of excise leviable thereon has been granted absolutely, the manufacturer of such excisable goods shall not pay the duty of excise on such goods. Sub-section (2) empowers the Central Government to grant exemption from duty of excise by special order in each case under circumstances of an exceptional nature to be stated in such order. The Government however does not change any power under Section 5A(2) to exempt goods partly from duty, unlike the cases of General Exemptions under Section 5A(1). Further, whereas the exemptions given by the Central government under Section 5A(1) will be communicated through a notification published in the Official Gazette, the exemptions given under Section 5A(2) will be communicated through special orders.

Sub-section (2A) to Section 5A empowers the Central Government to insert an explanation to such notification or order issued under Sub-sections (1) or (2) for the purpose of clarifying the scope or applicability of the notification / order as the case may be, by way of notification in the official Gazette at any time within one year of the issue of above notification/order.

Every such explanation shall have effect as if it had always been the part of the notification issued or order passed under Sub-sections (1) and (2) of Section 5A of the Act, which means, it has retrospective effect.

While the Government is thus empowered to give duty relief through exemptions, the question arises whether utilising this instrument, the Government can change the rate structure itself. They can do so, since Section 5A(3) states that through exemptions, rates of duty may be prescribed in 'a form or method' different from what obtains in the statutory rate. Thus, while the statutory rate may be on the basis of value (ad valorem rate), through an exemption, it may be converted into a rate based on quantity (specific rate) or vice versa. The important condition is that by such conversion through exemptions, the quantum of duty should not exceed what is authorised by the statutory rate. The parliamentary control over taxation is supreme and inviolable.

Sub-section (4) of Section 5A provides that every notification issued under Sub-rule (1) and in force immediately before the commencement of the Customs and Central Excise Laws Amendment Act, 1988 shall be deemed to have been issued or made under the provisions of this section and shall continue to have the same force and effect after such commencement until amended, varied, rescinded or superseded under the provisions of Section 5 of the Central Excise Act, 1944.

As per Sub-section (5) of Section 5A, "every notification issued under Sub-section (1) or Sub-section (2) shall:

- (a) unless otherwise provided, come into force on the date of its issue by the Central Government for publication in the Official Gazette;
- (b) also be published and offered for sale on the date of its issue by the Directorate of Publicity and Public Relations, Customs and Central Excise,

New Delhi, under the Central Board of Excise and Customs constituted under the Central Board of Revenue Act, 1963 (54 of 1963).

As per Sub-section (6), notwithstanding anything contained in Sub-section (5), where a notification comes into force on a date later than the date of its issue, the same shall be published and offered for sale by the said Directorate of Publicity and Public Relations on a date on or before the date on which the said notification comes into force.

In order to put the matter beyond all doubt and minimise disputes it is statutorily provided that unless it is specified otherwise, an exemption notification shall come into effect on the date of its issue. As stated earlier this is to remove the practical problem resulted by the Supreme Court judgement in *Collectors v. New Tobacco Co.* - 1998 (97) E.L.T. 388 (S.C.).

6.11.4 Statutory control over Government's power to exempt

While the government has been given the power to reduce rates of duty as against what is fixed by the legislature, still, the law has made provisions, for a close vigil being kept over executive action in such areas. Section 38 of the Act requires all notifications being published in the Official Gazette by which, any exercise of the power to exempt goods from duty becomes a matter of public knowledge. Moreover, machinery exists to enable the Parliament to monitor the manner in which the exempting power is used. The Comptroller and Auditor General of India, acting as an independent agency to safeguard revenue interests, highlights in his Annual Report (known as Audit Report) the extent of revenue sacrifice made during the year through exemptions in operation. This report is subject to close scrutiny and comment by the Public Accounts Committee of the Parliament. This is a price publication i.e. sold to the public. Thus, the principle of accountability of the Government to the public is also achieved. Democracy is, after all, 'Open Government'.

6.11.5 Types of exemptions

Exemption notifications issued by the Central Government under Section 5A(1) of the Central Excise Act, 1944 fall into different categories.

Specific Exemptions: Exemptions normally give duty relief to the goods specified in the text of the notifications attracting a specific rate of duty as per classification under a particular heading in the Tariff. These are known as 'specific exemptions' and in the Tariff Schedule, they are printed in the Chapter relevant to the goods being exempted.

General Exemptions: In contrast, a number of exemptions have been issued whose coverage extend to goods falling in several chapters in the tariff, and these are known as 'general exemptions'. These are printed in a separate portion of the tariff.

Exemptions, whether specific or general which do not specify any condition to be fulfilled for purposes of availing the benefit are known as 'straight' or unconditional exemptions. On the other hand the exemption benefit may be subject to the fulfilment of certain conditions specified in the notification itself, in which case it is known as a 'conditional exemption'.

Normally, exemption notifications do not specify the date upto which the benefit is available, and hence the assessee can obtain the benefit till such time as the exemption is alive, and the benefit will cease only from the date on which the exemption is rescinded. However, in a few cases, the exemption notification itself will incorporate the date upto which the notification will be in force. These are known as 'time bound exemptions'. The deadlines specified in the Notification in such cases may however be extended by the Central Government through amending notifications. Such amending notifications should have been issued before the expiry of the original deadline.

6.11.6 Procedure for availing exemptions

What an exemption does is to reduce the duty liability for what has been prescribed in the statutory rate. Hence, wherever an exemption is availed, the rate prescribed in the exemption notification alone becomes operative for the goods to be assessed and it is hence known as an "effective duty". The rate given in the exemption is also known as "exempted rate" or "concessional rate". Determination of the rate of duty chargeable on excisable goods is of crucial significance.

The manufacturer intending to avail the benefit of exemption notification issued under Section 5A of the Central Excise Act, 1944 in respect of subject goods for specific use at concessional rate of duty as per Central Excise (Removal of Goods at Concessional Rate of Duty for Manufacture of Excisable Goods) Rules, 2001 is required to make an application in quadruplicate, to the jurisdictional Assistant/Deputy Commissioner of Central Excise. Separate application shall be filed by the manufacturer in respect of each supplier of subject goods.

A bond in the prescribed form is required to be executed with such surety/security as the Assistant/Deputy Commissioner may prescribe having regard to the duty liability estimated to be involved at a given time.

The aforesaid application shall be countersigned by the Assistant/Deputy Commissioner, who shall certify therein that the said person has executed a bond to his satisfaction in respect of end use of the subject goods and indicate the particulars of such bond. One copy of the application shall be forwarded to the jurisdictional range superintendent of the manufacturer of the subject goods, two copies shall be handed over to the manufacturer and one copy shall be retained by the Assistant/Deputy Commissioner. Out of the two copies with the manufacturer, he shall forward one copy to the manufacturer of subject goods.

As per Rule 4 of the Central Excise (Removal of Goods at Concessional Rate of Duty for Manufacture of Excisable Goods) Rules, 2001, the manufacturer of subject goods shall avail the benefit of exemption notification on the basis of the application so made and shall record on the application the removal details, such as No. and date of invoice, description, quantity and value of subject goods and amount of excise duty paid at concessional rate.

Goods detained by the manufacturer at concessional rate of duty shall be properly accounted for and shall be used only for the purpose for which they are brought. For this purpose a simple account indicating quantity and value of subject goods, quantity consumed for intended purpose and quantity remaining in stock is

required to be maintained invoice-wise and also a monthly return shall be submitted to the Assistant/Deputy Commissioner by the tenth day of the following month.

It has been laid under Rule 6 of these Rules where the subject goods are not used by the manufacturer for the intended purpose, he shall be liable to pay the amount equal to the difference between the duty leviable on such goods but for the exemption and that already paid if any at the time of removal from the factory of the manufacturer of the subject goods, along with interest and the provisions of Sections 11A and 11AB of the Central Excise Act, 1944 shall apply mutatis mutandis for effecting such recoveries.

It has been clarified by an Explanation appended to Rule 6 of the Rules that subject goods shall be deemed not to have been used for the intended purpose even if any of the quantity of the subject goods is lost or destroyed by natural causes or by unavoidable accidents during transport from the place of procurement to the manufacturer's premises or during handling or storage in the manufacturer's premises.

6.11.7 Duty exempted goods exempted from Registration

All the producers, manufacturers and wholesale dealers in excisable goods are required to obtain 'registration certificate' in terms of Section 6 read with Rule 9 of the Central Excise Rules, 2002. However, a registration obtained under erstwhile Rule 174 of the Central Excise Rules, 1944 or rule 9 of the Central Excise (No.2) Rules, 2001 shall be deemed to be as valid as the registration made under Rule 9(1) of the Central Excise Rules, 2002. Relaxation is available to manufacturers of goods which are exempted from duty under Section 5A of the Central Excise Act, 1944. Rules 9(2) and 9(3) empowers the Central Board of Excise and Customs to grant exemption from registration for manufacturers of goods which are exempted from duty, by notification in Official Gazette, subject to such conditions and limitations as may be specified.

6.11.8 Scope of Exemption Notifications

Whenever any duty exemption is granted through a notification issued in the Gazette of India, the rate prescribed therein is applicable in respect of removals made on or after the date of the Gazette in which it is published. However, in rare cases, the Government has also issued notification taking effect on a future date. For instance, Notification No. 76/86, though it was issued on 10.2.86 came into force only on 28.2.86 as specifically provided for in the notification itself. Thus, exemptions while they normally take immediate effect, occasionally take effect from a date subsequent to the date of issue. While exemptions can thus have only prospective effect, there have been a few rare occasions where retrospective effect was given for certain exemptions. However, the judiciary on several occasions pronounced such practices as bad in law.

The dispute has, however, been set at rest by the decision of the Supreme Court in the case of *Wallace Flour Mills Co. Ltd. v. Collector of Central Excise* (1989) 44 ELT 598 (SC). The position in law therefore is that while the taxable event no doubt may be the actual manufacture of the goods under assessment, the rate of duty applicable is the rate prevailing on the date of its actual removal from the factory or the warehouse where non duty paid stock is stored.

6.12 Recovery of Sums Due to Government (Section 11)

Section 11 contains the provisions relating to recovery of sums due to the Government. This section covers recovery not only of duties but even of “any other sums of any kind” payable to the Central Government under the Central Excise Act and Rules. Sums due to the Government including those arising out of duty demands confirmed under Section 11A are to be paid by the assessee immediately. If any amount is due to the assessee (i.e. refunds), Section 11 authorises the department to set off the amount demanded from the assessee, against refunds due to him. If the amount is not paid, the section authorises recovery of the amount by attachment and sale of excisable goods belonging to the assessee. If the amount is not so recovered, the department will resort to what is known as “certificate action”. This would mean that the Assistant Commissioner will prepare a certificate signed by him, specifying the amount due from the assessee and send it to the Commissioner of the Revenue District in which the assessee resides or conducts his business. This District Commissioner is empowered by Section 11 to proceed to recover the amount as if the amount constituted arrears of land revenue. Where a person from whom some recoveries are due, transfers his business to another person, then the excisable goods, plant, machinery etc., in the possession of the transferee can be attached and sold for recovery.

Normally, assessees in Central Excise do honour the demands. If they do not, methods as noted are available to recover the amounts through attachment or certificate action. However, there may be rare cases where despite all these measures, amounts are still not recoverable from the concerned parties. In such cases there is no option except for the department to write off the amounts as irrecoverable. Powers have been vested with the officers at different levels, to write off sums as not recoverable upto limits as specified in administrative instructions issued from time to time.

6.13 Recovery of duties not levied or not paid or short levied or short paid or erroneously refunded (section 11A)

The law authorizes the department to demand payment of duty arising in the cases mentioned below in the following manner:

- (a) Show cause notice (SCN) shall be served within one year from the relevant date where duty of excise not levied or not paid or short levied or short paid or erroneously refunded for reasons other than fraud or collusion or wilful misstatement or suppression of facts or contravention of any of the provisions of this Act or the rules made there under with the intent to evade payment of duty.

In such a case assessee may pay the duty before the service of notice along with the interest and inform the Central Excise Officer (CEO) in writing. On receipt of the information CEO may proceed for recovery of any shortfall of such amount by issue of SCN within one year from the date of receipt of such information.

- (b) Show cause notice shall be served within 5 years from the relevant date where duties not levied or not paid or short levied or short paid or erroneously refunded by reasons:
 - (i) fraud or

- (ii) collusion
- (iii) wilful misstatement
- (iv) suppression of facts or
- (v) contravention of any of the provisions of this Act or the rules made there under with the intent to evade payment of duty.

The notice shall specify the amount of duty along with interest under section 11AA and penalty equivalent to the duty.

- (c) Show cause notice shall be served within 5 years from the relevant date, where during the course of any audit or investigation or verification it is found that any duty has not been levied or paid or has been short levied or short paid or erroneously refunded due to fraud or collusion or wilful misstatement or suppression of facts or contravention of any of the provisions of this Act or the rules made there under with the intent to evade payment of duty but the details relating to transaction are available in the specified records. The notice shall specify the amount of duty along with interest under section 11AA and penalty equivalent to the 50% of such duty.

In such a case assessee may pay the duty before the service of notice along with the interest and penalty equal to 1% of such duty per month to be calculated from the month following the month in which duty was payable but the amount of penalty shall not exceed 25% of the duty and inform the Central Excise Officer (CEO) in writing. On receipt of the information CEO may proceed for recovery of any shortfall of such amount by issue of SCN within one year from the date of receipt of such information.

Where the service of is stayed by a court or tribunal, the period of such stay shall be excluded in computing the period of 1 year or 5 year as the case may be.

After considering the representation made by the assessee the CEO shall determine the amount of duty payable which shall not exceed the amount specified in the notice within;

- 6 months from the date of notice for cases mentioned in point (a).
- 1 year from the date of notice for cases mentioned in point (b) & (c).

“Relevant date” for the purpose of this section means:

- (a) *in the case of excisable goods on which duty of excise has not been levied or paid or has been short-levied or short paid:*
 - (i) *where under the rules made under this Act a periodical return, showing particulars of the duty paid on the excisable goods removed during the period to which the said return relates, is to be filed by a manufacturer or a producer or a licensee of a warehouse, as the case may be, the date on which such return is so filed;*
 - (ii) *where no periodical return as aforesaid is filed, the last date on which such return is to be filed under the said rules;*
 - (iii) *in any other case, the date on which the duty is to be paid under this Act or the rules made thereunder;*

(b) in a case where duty of excise is provisionally assessed under this Act or the rules made thereunder the date of adjustment of duty after the final assessment thereof;

(c) in the case of excisable goods on which duty of excise has been erroneously refunded, the date of such refund.

“Refund” includes rebate of duty of excise on excisable goods exported out of India or on excisable material used in the manufacture of goods which are exported out of India.

“Specified Records” means records including computerized records maintained by the person chargeable with duty in accordance with any law for the time being in force.

6.14 Interest on Delayed Payment of duty (Section 11AA):

The person who is liable to pay duty shall also be liable to pay interest at the rate not below 10% and not exceeding 36% as may be fixed by the Central Government. Such interest shall be paid from the date on which such duty becomes due to the date of actual payment.

However, no interest shall be payable where;

- (a) duty becomes payable consequent to the order, instruction, direction by the Board under section 37B and
- (b) such amount is paid voluntarily in full within 45 days from the date of issue such order, instruction, direction without reserving any right to appeal.

Penalty for short levy or non-levy of duty in certain cases (Section 11AC)

The person who is liable to pay duty shall also be liable to pay penalty:

- (i) equal to the amount determined by the CEO under section 11A, where duty not levied or not paid or short levied or short paid or erroneously refunded due to fraud or collusion or will misstatement or suppression of facts or contravention of any of the provisions of this Act or the rules made there under with the intent to evade payment of duty.
- (ii) equal to 50% of the duty determined by the CEO under section 11A, where during the course of any audit or investigation or verification it is found that any duty not levied or not paid or short levied or short paid or erroneously refunded due to fraud or collusion or will misstatement or suppression of facts or contravention of any of the provisions of this Act or the rules made there under with the intent to evade payment of duty but the details relating to transaction are available in the specified records. However, if the duty determined is paid within 30 days of the date of communication of the order the penalty liable to be paid shall be 25% of the duty so determined only in a case where the penalty is paid within the period so specified.

6.15 Claim for refund of duty and interest, if any, paid on such duty (Section 11B)

Any person claiming a refund may make an application to the Asstt./Deputy Commissioner in the prescribed format within one year from the relevant date and

the application should be accompanied by documentary or other evidence in order to establish that the amount of duty of excise and interest, if any, paid on such duty with regard to which the refund is claimed was collected from or paid by the applicant and that the incidence of such duty had not passed on by him to any other person.

Limitation of one year shall not apply where any duty and interest, if any, paid on such duty has been paid under protest.

The Asstt./Deputy Commissioner will adjudicate the refund claims filed by the applicant and if he is satisfied that the whole or any part of the excise duty which was paid by the assessee is refundable he may make an order accordingly and amount so determined shall be credited to the fund. The Fund has been since constituted is known as Consumer Welfare Fund.

However the refund shall be granted to the applicant instead of being credited to the Fund, if the refund pertains to:

- (a) rebate of excise duty on exported goods or rebate of excise duty on materials used in the manufacture of exported goods;
- (b) outstanding balances in the Account Current;
- (c) refunds of CENVAT credit on excisable goods used as inputs;
- (d) duty of excise paid by the manufacturer if the incidence of such duty has not been passed on by the manufacturer to any other person;
- (e) the duty of excise borne by the buyer, if the incidence of such duty has not been passed on the buyer to an other person;
- (f) the duty of excise borne by any class of applicants as may be notified by the Central Government.

Refunds shall only be granted if the amount relatable to the above (a) to (f), notwithstanding anything contrary contained in such judgment, decree, order or direction of the Appellate Tribunal or any Courts or in any provisions of the Act and Rules or in any other law for the time being in force.

'Relevant date' has been defined as follows:

- (a) *in the case of refund of duties on exported goods or inputs used in the manufacture of such goods, the date on which the export has taken place i.e. the date on which the ship or air craft in which the goods are exported leaves India or the date on which such goods physically pass the customs frontiers of India in case of export by land and if exported by post the date of dispatch by the post office.*
- (b) *in the case of goods returned for remaking/reconditioning, the date of entry of goods into the factory for the aforesaid purpose;*
- (c) *in the case of goods to which banderols are required to be affixed if removed for home consumption but not so required when exported outside India, if return to a factory after having been removed from such factory for export out of India, the date of entry into the factory;*

- (d) *in a case where a manufacturer is required to pay a sum, for a certain period, on the basis of the rate fixed by the Central Government by notification in the Official Gazette in full discharge of his liability for the duty leviable on his production of certain goods, if after the manufacturer has made the payment on the basis of such rate for any period but before the expiry of that period such rate is reduced, the date of such reduction;*
- (e) *in the case of a person other than the manufacturer, the date of purchase of goods by the person;*
- (ea) *in the case of goods which are exempt from payment of duty by a special order issued under Sub-section (2) of Section 5A, the date of issue of such order;*
- (eb) *in case where duty of excise is paid provisionally under this Act or the rules made thereunder, the date of adjustment of duty after the final assessment thereof;*
- (ec) *where refund arises due to order of appellate authority, tribunal or court, relevant date shall be date of such order;*
- (f) *in any other case, the date of payment of duty.*

“Refund” includes rebate of duty of excise on excisable goods exported out of India or on excisable material used in the manufacture of goods which are exported out of India.

6.16 Doctrine of Unjust Enrichment

If the manufacturer had charged the excise duty of his buyer then refund of excise duty paid to the manufacturer will amount to excess profit to him, therefore, it will not be reasonable to refund duty to him as he will get double benefit first from the customer and again from the Government this is called Unjust Enrichment.

As per the principle of Unjust Enrichment the refundable amount will be credited to a Consumer Welfare Fund specified in section 12C and will be utilized for the purposes of and in the manner specified in Section 12D. However, section 11B prescribed certain situations in which refund of the duties of excise paid can be made, to an applicant.

6.17 Payment of Interest on delayed Refund (Section 11BB)

Section 11BB of the Central Excise Act, 1944, provide for payment of interest on refunds of duty which is not paid to the applicant within three months from the date of receipt of application under Sub-section (1) of Section 11B of the Act. Interest shall be payable at the rate not below 5% and not exceeding 30% p.a. as may be fixed by the Central Government from the *date of the expiry of the 3 months from the date of receipt of application till the date of refund.*

6.18 Power not to recover duty of excise not levied or short-levied as a general practice (Section 11C)

The need for demanding duty under Section 11A naturally arises due to amounts of duty not being charged or paid correctly. One of the several reasons which can

give rise to the original error could be a wrong interpretation of the Central Excise Law, including the tariff and notification. While individual errors of this nature are no doubt rectified through demands under Section 11A, it may occasionally happen that the erroneous interpretation of law conferring the undue benefit to the assessee, was in fact not confined to a few sporadic cases, but the error was fairly widespread. Such an erroneous "general practice", if it is to be rectified through demands, may not be fair to the industry and trade, particularly since excise is an indirect tax and whatever amounts are paid by the assessee, are passed on and recovered from the consumers. Wherever retrospectively such assessments are re-opened there is an element of inequity in that the assesses have no means of recovering the extra amounts from the market where the goods in question already stand sold. Taking this into consideration, a new provision was introduced on 1.7.1978 as Section 11C. This section authorises the Central Government not to recover duties, if the amounts in question are due to errors in interpretation of the law which errors were not stray or sporadic. But were ubiquitous, and thus constituted a "general practice". In such situations, Section 11C authorises the Government to issue a notification in the Gazette directing non-recovery of the sums.

The section clearly meant to provide equitable relief to assesses who had in good faith paid less duty than was legally due. Where duty was fully recovered as due under the law at the time of clearance then refund of duty paid shall be granted in accordance with section 11B. However in such case an application shall be made *before the expiry of six months from the date of issue of such notification.*

6.19 Excise Audit—2000

In the Budget proposals for the Financial year 1996-97, the Finance Minister announced that a 'scheme of selective audit by the excise officers' in place of the then existing internal audit would be started. Instructions regarding this 'Selective' Audit were later issued by the CBEC in November 1996 vide Circular No. 267/101/96-CX, dated 13.11.1996. This audit was primarily directed at units other than SSI units and medium units paying annual revenue of less than Re. one crore, and it envisaged an in-depth scrutiny of the statutory records and returns.

In October 1999, the Department decided to 'have a more scientific and effective audit system by professionally trained officers', and introduced a 'New Excise Audit System Code' named as 'Excise Audit—2000' (EA-2000). Instructions and guidelines regarding this system were issued by CBE&C vide Circular No. 491/57/99-CX, dated 28.10.1999, and No. 514/10/2000-CX, dated 16.2.2000.

As per the details circulated by the Department, the Excise Audit—2000 introduced with effect from 15th November, 1999 have the following main features:

- A minimum of 15 days notice should be issued to the concerned assessee before commencing any audit.
- The actual audit shall commence w.e.f. 1st December, 1999.
- It is not an Additional Audit but only a modification of existing internal audit system.
- Emphasis under this audit has been made on scrutiny of business records of the company/assessee rather than statutory records.

It is separate from "Special Audit" under Sections 14A and 14AA of the Act.

Excise Audit shall be conducted in the following manner:

- (1) Once in every year where the amount of duty paid i.e. cash + CENVAT credit by assessee is more than ₹3 crores.
- (2) Once in two years, where duty paid is between ₹1 crore and ₹3 crore.
- (3) Once in five years, where duty paid is between ₹50 lakhs and ₹1 crore.
- (4) 10% of units every year where the duty paid is less than ₹50 lakh.

Units already audited in the current financial year under the existing audit system shall continue to be audited as per existing Audit Manual.

It is a Departmental audit conducted by auditors who are excise officers and Assistant Director (Costs) who are Cost Accountants by qualification and are specially trained for this purpose. Assistant Director (Costs) shall conduct this audit in major units.

The main thrusts of Excise Audit is :

- to improve the present audit system;
- adoption of Information Technology in auditing;
- preparation of Manpower for Service Tax Audit;
- procedural relaxations in excise law;
- to provide tools for uniform decision making with the help of Information Technology;
- optimal use of manpower in audit.

This audit shall be conducted with the help of Audit Manual, Standard Audit Programme and Working Papers. The Audit Manuals will lay down audit standards, instructions, policies and procedures relating to audit of an assessee and ensure that audits are uniform, comprehensive and efficient in accordance with the standards laid therein.

Standard audit programme is a systematic and comprehensive sequence outlining the procedure for conduct of audit in order to arrive at an opinion concerning the degree of compliance by the assessee to the law and procedure. And working papers details the work done by the audit party in the given format and shall be filed by the Supervisors of the Audit team. There will be a set of working papers for each item of work/verification done by the auditors.

This audit is required to be completed within 5 to 7 working days. This period may be extended in exceptional cases. To keep the number of days for audit within a reasonable limit, the Commissioner may enhance the strength of the audit team or depute two audit teams clearly specifying its functions.

6.20 Deposit of Central Excise Duty During Strikes in Nominated Banks

“Doubts have been raised about the payment of Central Excise duties during strikes etc. in the Nominated Bank after commencement of the scheme of “one bank one Collectorate” w.e.f. 1.4.86. It is clarified for the information of the Trade that the procedure being followed earlier in such circumstances may be followed even-after introduction of “one bank one Collectorate”. The procedure to be followed is appended herewith.

Procedure for deposit

Normally, in all cases of closure of Bank business due to strike by bank employees, the public get advance intimation either through the Press or otherwise. In all such cases, the assesseees are required to make advance arrangements to deposit moneys into the Banks and keep sufficient amounts in their PLAs so that they do not face any difficulty in the clearance of the goods during the period of strike.

In cases where the strike of Bank employees is without notice, or where the strike after due notice is prolonged beyond a reasonable time (say over 3-4 days), a Special Trade Notice will be issued specifically by this office, adopting the following procedure, in partial relaxation of the existing procedure, only for the duration of such sudden strike without notice.

Only on issue of such a Trade Notice by this office on such special and specific occasions during the days of closure of Bank business on the dates, (as may be specified in such a Trade Notice where possible) the assessee can send their cheques by Registered Post Acknowledgement Due (RPAD) or through special messenger, with TR-6 challans (in quadruplicate) to the Chief Accounts Officer, Central Excise Hdqrs. Office, Bombay-III Collectorate, Navprabhat Chambers, Ranade Road, 2nd Floor, Dadar - 28, alongwith a forwarding letter containing also a clear declaration that they have sufficient balance in their bank account. Assessee will be advised to send a copy thereof to the concerned jurisdictional Range Officer also. On the strength of a cheque so sent, they may take credit in the PLAs and clear the goods. In the absence of any such specific Trade Notice, the assessee will have to ensure advance deposits in the nominated banks functioning, even though one or some (not all) of the nominated banks go on strike. They should neither send cheques to Chief Accounts Officer nor take credit on the basis of any such cheque so forwarded.

On receipt of the cheque in CAO's Office, CAO will advise the concerned R.O. (Range Officer) about the name of the assessee, the No. and date of the cheque and its amount. Immediately after the strike is over, all such cheques would be deposited by the CAO into the Focal Point Bank, through TR-6 challans in quadruplicate according to the procedure prescribed. On release of the challans by the F.B. (Focal Bank) to the Chief Accounts Officer on realisation of the cheque, the duplicate/triplicate copies of the receipted challans will be sent by the Chief Accounts Officer to the assesseees concerned for their reference and record and for preparing the necessary monthly statement etc. Bank commission or collection charges, if any, on intimation, if any, by the CAO to the assesseees, as also to R.Os. It may be noted that if any of the cheques sent by the assesseees are dishonoured or returned by the F.B. for any other reason, the concerned licensee will be liable to such penal action as prescribed under the erstwhile Central Excise Rules, 1944, and as may be considered necessary, including prosecution, if necessary.

It may also be noted that the concession envisaged above cannot be extended to assesseees who work on overdrafts on their banks and are not able to give the required declaration along with the cheque that they have sufficient balance in their accounts in the bank to meet the amount of the cheque. Any false declaration if so given, will be construed as a violation of the rules and procedure and the assessee will be liable to penal action under the rules.

Further Clarification

For removal of doubts and to ensure uniformity of application of the procedure laid above it is further clarified as follows:

- (a) the said procedure will be permitted to be followed by assessee on issue of a special Trade Notice for this purpose, only when all the banks nominated to collect revenue within this Collectorate are unable to transact business, due to strike etc. In other words, if there is a strike in only one nominated bank, the assessee should still be in a position to deposit in the other nominated banks and consequently in such situation, the assessee will not be given the benefit of the above procedure.
- (b) The procedure referred to above will not be applicable:
 - (i) In the case of declared Bank Holidays, as such holidays are known in advance.
 - (ii) Where the Public has been given advance intimation of strike, unless the strike is unduly prolonged (say over 3-4 days).
 - (iii) Where the Bank employees adopt "go-slow" tactics.
 - (iv) In the case of closure of the assessee's Bank, unless that bank is the only nominated bank in the Collectorate.

It is once again stressed that no deviation from these instructions will be allowed without prior approval of this notice. (Bombay-III Collectorate Trade Notice No. 38/86, dated 4.6.1986).

6.21 Appellate Procedures and Search, Seizure and Investigation

Excise law makes elaborate provisions for departmental adjudication, appeals and revision.

Decisions made or orders passed by Officers of Central Excise at different levels can give rise to grievances which broadly are of two kinds. First, if the decision denies to the assessee the benefit due, or confers a hardship undue, it can create a grievance to him. Secondly, the decisions can confer on the assessee a benefit undue or deny revenues due to the Government, in which case the Government itself becomes the aggrieved party. There are two parties to every dispute, and it happens at times that satisfaction to one could mean dissatisfaction to the other. There should be mechanism to go into grievances of either kind and the appellate mechanism is meant precisely for that.

The judiciary is no doubt the agency before which relief can be sought by the citizen in matters of implementation or enforcement of any law, including laws pertaining to Central Excise and Customs. However, fiscal statutes like the Central Excise Act, 1944 and the Customs Act, 1962 contain provisions and constitute organisations within the departments themselves to enable settlement of such disputes, if possible, without the need to seek judicial remedy. The need for fiscal enactments to provide "in house" facilities, so to say, to seek redressal of grievances arises due to the fact that by the very nature of such laws, and the dimensions of the field that they cover, the number of disputes which emerge is so huge as to make it a

very difficult proposition for the judiciary alone to deal with. Further, the judicial process is expensive and time consuming and hence unviable if the judiciary alone is made the resort to citizens. Statutory provisions pertaining to appeals are contained in Chapter VI-A of the Central Excise Act, 1944 (Sections 35 and 36) inserted by the Finance Act, 1980 and came into force on 11.10.1982.

6.21.1 Appellate Scheme

The appellate scheme in Central Excise comprises three institutions viz. Commissioner (Appeals); the Customs, Excise and Service Tax Appellate Tribunal (CESTAT); and the Government of India as revisionary authority. The principle inbuilt into the scheme is that for an appeal to lie before a particular authority, it should have been passed by authorities lower in rank within the department to the appellate authority. The table below, bringing out the stages of appeal in regard to orders passed by each authority will indicate how this principle is incorporated in the appellate scheme.

	<i>Orders passed by</i>	<i>Relief at first stage</i>	<i>Relief at second stage</i>
(a)	Superintendent/Assistant Deputy/Additional/Joint Commissioner	Appeal before Commissioner (Appeals)	Appeal before CESTAT
(b)	Commissioner	Appeal before CESTAT	Appeal before CESTAT

6.21.2 Appeals before Commissioner (Appeals)[Section 35]

Under Section 35(1) any person aggrieved by any decision or order passed under the Act by an officer lower in rank than a Commissioner may appeal to the Commissioner (Appeals). The time limit for filing an appeal is sixty days from the date of communication of the order contested. The word "communication" used in this section would mean actual receipt by the appellant, of the order impugned. The Commissioner may adjourn an appeal or grant time to parties as the case may be. However, no such adjournment shall be granted more than three times to a party during hearing of the appeal. Commissioner (Appeals) has no powers to relax the time limit further.

Procedure for filing Appeal before Commissioner (Appeals)

The appeal should be filed in Form EA-I in duplicate and should be accompanied by a copy of the order or decision appealed against. While the statutorily prescribed form should invariably be filed, if the appellant desires to make his grounds more elaborate, there is no bar to his doing so by attaching extra sheets. In his own interest, the appellant must make his case in a clear, comprehensive and self-contained manner, adducing all the arguments and submitting all the evidence along with the appeal. However, if compulsions of time limit for filing the appeal render this difficult, he may make a suitable indication in the appeal that further elaboration/evidence will be sent separately. If the constraints of the columns in the prescribed form render it difficult to explain the grounds, an indication can be made in the form to the effect that the grounds of appeal are enclosed, and the grounds can be elaborated in separate sheets annexed to the proforma. The requirement is only that without the proforma duly completed, the appeal will not be accepted.

While filing the appeal which can be either by tendering it in the Office of the Commissioner (Appeals) or by sending it by Registered Post Acknowledgement Due, the appellant must make sure that in either case, he gets possession of a dated acknowledgement of receipt. This is of crucial importance since if the appeal is time barred, it will be rejected on that ground alone, without the merits being looked into.

Apart from making the grounds in writing, the appellant can also seek the facility of being heard in person by the Commissioner (Appeals) before the appeal is decided upon. Section 35-A(1) makes it mandatory that personal hearing should be granted whenever asked for. For the hearing, the appellant may either appear in person or through a counsel authorised for such purposes.

The appeal filed will be examined in the Office of the Commissioner (Appeals) on the basis of the records pertaining to the decision impugned. If a personal hearing has been asked for, the Commissioners (Appeals) will decide the date and time, and an intimation sufficiently in advance will be sent to the appellant/counsel. Failure to present oneself for personal hearing on the date and time fixed may result in the appeal being decided on the basis of the written plaint alone.

However, if there are any insurmountable difficulties in appearing on the date, intimation should be given to the Commissioner (Appeals) before the date fixed for hearing, and a revised date/time is requested for and obtained.

Even if a counsel is engaged, there is no bar to the appellant also presenting himself and explaining his case. A record of the submissions made during the hearing will be made, and this will form an integral part of the appellate order eventually issued. The practice followed by most Commissioners (Appeal) is to make a record of the hearing and obtain the signature of the party heard thereon before proceeding to decide the appeal. This should give satisfaction to the appellant that the record reflects all the submissions made, in a correct manner. If the appellant feels that the record does not correctly reflect all the arguments made during the hearing, he would be well advised to bring this immediately to the notice of the Commissioner (Appeals) for rectification of the record.

While normally, a personal hearing is meant for elaboration of the grounds already made in the written plaint, Section 35-A(2) authorises the Commissioner (Appeals) at the time of hearing of the appeal, to allow the appellant even to go into grounds not specified earlier in the written appeal, provided the Commissioner (Appeals) is satisfied that the omission of the ground earlier was not wilful or unreasonable.

After the hearing is completed, the Commissioner (Appeals) will decide the case on the basis of all the facts and evidence on record and issue the order in appeal. It should be a "speaking order" in the sense that not only the decision but also the detailed reasoning for the decision should be incorporated therein and communicated to the appellant. Section 35-A(4) makes this a statutory requirement.

The order issued by the Commissioner (Appeals) may confirm, modify or annul the order appealed against (the original order) as provided in Section 35-A(3) after such inquiry as he may think just and proper. While any appellate order confirming, modifying or annulling the original order implies that the appeal is decided on merits, the Commissioner (Appeals) may also refrain from doing these. Section 35-A(3) authorises him even to refer the case back to the original authority, with such directions as he thinks fit, for a fresh decision, with or without the original authority

taking additional evidence if necessary. Normally this practice of remanding cases for de novo decision is resorted to in cases where the Commissioner (Appeals) is of the view that the original authority had not adhered to the principles of natural justice, or fresh evidence had been adduced at the appeal stage which the Commissioner (Appeals) deems it fit should be looked into by the original authority first. While appeals are normally filed seeking relief, there is no bar to the Commissioner (Appeals) not only giving relief, but even causing further privations to the party. The two provisos to Section 35A(3) authorise this. The Commissioner (Appeals) can enhance any penalty or fine or confiscate goods of value greater than what had been confiscated by the original authority, or reduce the amount of refund. However, if he contemplates taking any such action, it can only be after putting the appellant on notice, and giving him reasonable opportunity to oppose the proposed decision. Similarly, the Commissioner (Appeals) if he is of the opinion that certain duties are due to the department but had not accrued, can order payment of such sums, provided a notice is issued for demanding the duty within the time limit prescribed under Section 11-A. As provided in Section 35A(4A), the Commissioner (Appeals) may, where it is possible to do so hear and decide every appeal within a period of six months from the date on which it is filed.

6.21.3 CESTAT

To ensure safeguards to citizens' interests in any area of administration, including fiscal administration, it is essential that appellate authorities are totally independent of the administrative authorities. Till a few years back, the appellate mechanism in Central Excise was liable to critical comment in this regard, since the appellate remedies then provided in the statute culminated in the Central Board of Excise and Customs itself acting as an appellate agency. The Board, in this manner, combined the functions of the administrative as well as the appellate authority in the department. Though the Board, manned by very senior officers in the department, maintained the highest standards of objectivity in considering appeals, was still prone to give rise to widespread misgivings in the minds of trade and industry regarding the possibility of a 'revenue bias' in its approach as an appellate body. A number of Committees and Commissions set up by the Government from time to time, such as the Central Excise Reorganisation Committee, the Tariff Revision Committee, etc. took stock of the position and suggested the setting up of an independent Tribunal on the lines already available in regard to Income Tax, so that such misgivings may be dispelled, and confidence created in the minds of the assessees as a whole.

The department eventually decided to set up the Tribunal and the necessary legislation was made in 1980 [Section 50 of the Finance (No. 2) Act, 1980]. The legislation was implemented from 11.10.1982, the date of implementation being announced through Notification No. 214/82-CE dated 10.9.1982.

The Tribunal can also deal with the cases under service tax. However, it is not vested with the powers of review.

(1) Composition of the Tribunal

As with the Income Tax Appellate Tribunal, CESTAT comprises technical members and judicial members, the underlying idea being that the former would provide the forum, the benefit of their knowledge and experience in the Department, and the latter will contribute benefits arising from unalloyed judicial approach. At present, the CESTAT functions in Delhi, Kolkata, Chennai, Mumbai and Bangalore.

The CESTAT is presided over by a President, with one or more Vice Presidents. As for members, the technical members are very senior officers of the rank of Commissioners of Central Excise and Customs, whereas the judicial members are senior members of the bench or the bar, selected for appointment.

As indicated in the statement at the very beginning, appellate orders decided by Commissioners (Appeals) can be contested before the CESTAT and in such situations, it functions as a second appellate forum. Original orders passed by Commissioner (including Additional Commissioner) can be contested straightaway before the CESTAT. In such situations, it will function as the first and the only appellate forum within the department. Appeals are normally decided on the basis of majority decision. In case a major decision does not arise, the President can nominate an extra member to the bench, to enable a majority decision arising.

To ensure that the valuable time of a body of this nature is not wasted in examining disputes involving insignificant stakes, it has been provided that the CESTAT may, in its discretion, refuse to admit the appeal in respect of any order if the amount of fine or penalty under contest does not exceed ₹ 50,000/- (Rupees Fifty Thousand only) [Section 35B(1)]. However, if the issue involved pertains to determination of the rate of duty or valuation, the CESTAT cannot refuse to admit the appeal, whatever be the amount involved. Again, to ensure optimum utilisation of the Tribunal's valuable time, Section 35D(3) provides that if the case involves amounts upto ₹ 10,00,000/-(Rupees Ten Lakh only) in duty/fine/penalty, a single Member (instead of a bench) can himself decide the case.

But where the amount involved is more than ₹ 10 crore on day to day basis, three member Benches shall be constituted for hearing such cases. All cases involving an amount of ₹ 25 crores or more would be listed before the Benches on priority basis and would be heard on day to day basis.

(2) Filing Appeal before CESTAT (Section 35B)

(1) Any person aggrieved by any of the following orders may appeal to the Appellate Tribunal against such order

- (a) A decision or order passed by the [Commissioner] of Central Excise as an adjudicating authority;
- (b) An order passed by the [Commissioner] (Appeals) under Section 35A;
- (c) An order passed by the Central Board of Excise and Customs constituted under the Central Boards of Revenue Act, 1963 (54 of 1963) (hereafter in this Chapter referred to as the Board) or the Appellate [Commissioner] of Central Excise under Section 35, as it stood immediately before the appointed day;
- (d) An order passed by the Board or the [Commissioner] of Central Excise, either before or after the appointed day, under Section 35A, as it stood immediately before that day.

Provided that no appeal shall lie to the Appellate Tribunal in respect of any order referred to in clause (b) if such order relates to loss of goods in transit, rebate of duty of excise on goods exported, goods exported outside India (except to Nepal or Bhutan) without payment of duty, credit of any duty allowed to be utilised towards payment of excise duty on final products under the provisions of this Act or the rules

made there under and such order is passed by the Commissioner (Appeals) on or after the date appointed.

Provided further that the Appellate Tribunal may, in its discretion, refuse to admit an appeal in respect of an order referred to in clause (b) or clause (c) or clause (d) where, the amount of fine or penalty determined by such order does not exceed fifty thousand rupees.

(2) The Committee of Commissioners of Central Excise may, if it is of opinion that an order passed by the Appellate [Commissioner of Central Excise under section 35, as it stood immediately before the appointed day, or the [Commissioner (Appeals) under section 35A], is not legal or proper, direct any Central Excise Officer authorised by him in this behalf to make an appeal to the Appellate Tribunal against such order.

Provided that where the Committee of Commissioners of Central Excise differs in its opinion regarding the appeal against the order of the Commissioner (Appeals), it shall state the point or points on which it differs and make a reference to the jurisdictional Chief Commissioner of Central Excise who shall, after considering the facts of the order, if is of the opinion that the order passed by the Commissioner (Appeals) is not legal or proper, direct any Central Excise Officer to appeal to the Appellate Tribunal against such order.

Explanation: For the purposes of this sub-section, "jurisdictional Chief Commissioner" means the Chief Commissioner of Central Excise having jurisdiction over the adjudicating authority in the matter.

(3) Every appeal under this section shall be filed within three months from the date on which the order sought to be appealed against is communicated to the Commissioner of Central Excise , or, as the case may be, the other party preferring the appeal.

(4) The party against whom the appeal has been preferred may file a memorandum of cross-objections within forty-five days of the receipt of the notice.

(5) The Appellate Tribunal can condone the delay in filing an appeal or memorandum of cross-objections if it is satisfied that there was sufficient cause for not presenting it within that period.

Fees:

An appeal to the Appellate Tribunal shall be in the prescribed form and shall be accompanied by a fee of:

- (a) Rupees one thousand where the amount of duty and interest demanded and penalty rupees five lakh or less.
- (b) Rupees five thousand, where the amount of duty and interest demanded and penalty levied is more than rupees five lakh but not exceeding fifty lakh rupees.
- (c) ten thousand rupees, where the amount of duty and interest demanded and penalty levied is more than fifty lakh rupees,

Provided that no fee shall be payable in the case where an appeal filed by the department or for submitting a memorandum of cross-objections.

(3) Appearance by Authorised Representative [Section 35Q]:

Both the parties to the dispute will be heard together by the bench. The Department will be represented normally by departmental officers functioning as Departmental Representatives. The assessee can appear in person or through counsel. In this regard, Section 35Q prescribes that any party to a dispute may otherwise than when required by the Tribunal to attend personally for examination on oath, can appear through an authorised representative who may be:

- (a) his relative or regular employee; or
- (b) Custom House Agent; or
- (c) any legal practitioner who is entitled to practice in any civil court; or
- (d) any person who has acquired such qualifications as the Central Government may prescribe by rules made in this behalf. The Central Government has since prescribed the qualifications under Rule 12 of the Central Excise (Appeals) Rules, 2001.

For the purposes of clause (c) of Sub-section (2) of Section 35Q, an authorised representative shall include a person who has acquired any of the following qualifications being the qualifications specified under clause (c) to Rule 12 of the Central Excise (Appeals) Rules, 2001, namely:

- (a) a Chartered Accountant within the meaning of the Chartered Accountants Act, 1949 (38 of 1949); or
- (b) a Cost Accountant within the meaning of the Cost and Works Accountants Act, 1959 (23 of 1959); or
- (c) a Company Secretary within the meaning of the Company Secretaries Act, 1980 (56 of 1980) who has obtained a certificate of practice under Section 6 of that Act; or
- (d) a post-graduate or an Honours degree holder in Commerce or a post-graduate degree or diploma holder in Business Administration from any recognised university; or
- (e) a person formerly employed in the Department of Customs and Central Excise or Narcotics and has retired or resigned from such employment after having rendered service in any capacity in one or more of the said departments for not less than ten years in the aggregate,

can act as an authorised representative.

(4) Decisions by CESTAT [Section 35C]

The orders passed by the Tribunal may confirm, modify or annul the order appealed against. The Tribunal may also refer the case back to the authority below which passed the order impugned, with such directions as it may deem fit, for fresh decision, taking additional evidence, if necessary. The Tribunal may also at any time within six months from the date of its own order, with a view to rectifying any mistake apparent from the record, amend any order passed by it, and can make such amendments as if the mistake is brought to its notice by Commissioner of Central Excise or the other party to the appeal.

Any amendment made in this manner under Section 35-C(2) enhancing the assessment or reducing the penalty can be made only after giving due notice to the other party.

The appeals shall be heard and decided by the Tribunal within three years from the date of filing of appeal. However, in case where stay order has been made in any proceeding relating to an appeal filed under Section 35B(1), the Tribunal shall dispose of the appeal within one hundred and eighty days from the date of such order. If the appeal is not disposed of within the above period, then on the expiry of the period, the stay order shall stand vacated [Section 35C(2A)].

CESTAT however, has the power to extend the stay beyond 180 days in deserving cases where delay was not attributable to the assessee, the same view was upheld by Supreme Court in *CCE v. Kumar Cotton Mills* 2005 (180) ELT SC.

The Honourable Supreme Court observed in the above case that the assessee cannot be punished for matters which may be completely beyond control.

No appeal can be filed against the order of the CESTAT granting or refusing stay because it is only an interim order.

However, if the Commissioner (Appeals) dismisses the appeal for non-payment of pre-deposit of duty pending appeal, it is a final order and appeal is allowed against such order before the CESTAT.

(5) Stay Petitions before CESTAT

While as with the Commissioner (Appeals), amounts to be paid as a consequence of the order disputed should be deposited even if an appeal is filed before CESTAT, the aggrieved party can however request the CESTAT for a stay of such deposits. The application for stay should be presented separately in triplicate by the appellant or his Counsel before the Registrar. Naturally, it should substantiate the request for stay with grounds, evidence etc. The applicant himself should serve one copy of the stay petition to the Senior Departmental officer representing the Department before CESTAT. This application for stay will be heard separately by the bench before the appeal is taken up for consideration. The other party (Department) can oppose the request, setting out the case why the requirement of deposit of duty/penalty etc. should not be stayed. The decision made by the bench to grant or refuse the stay is final.

After the appeal is decided, the Registrar will communicate the decision to the Appellant and the other party. The case records will be sent to the Excise Commissionerate to enable immediate implementation of the decision. In this regard, in cases where relief is given to the appellant by the CESTAT certain benches are known at times, to have fixed deadlines for implementation of decision giving relief. If such deadlines are breached by the department, the grievances in such matters can be agitated by the appellant before the concerned bench of the Tribunal.

6.21.4 Further Remedies after Decision by CESTAT

Orders of the Tribunal on points of facts are final. In all other matters, further remedies as below are available to the aggrieved parties.

1. Reference on Order of CESTAT

All orders made by CESTAT except those relating to classification and valuation will be appealable before the Honourable High Court if there is a substantial question of law under Section 35G.

Cases relating to classification and valuation shall be taken up directly to the Supreme Court.

The jurisdiction of the High Court to hear appeals continues till the National Tax Tribunal comes into operation.

The appeal shall be made before the Honourable High Court within 180 days of order of CESTAT.

The appeal will be heard by at least by a Division Bench of High Court. In case of difference of opinion by a division bench, it will be referred to the third judge and the majority of the opinion shall prevail.

2. Appeals and Constitutional Remedies

Appeal to Supreme Court can be made in the following cases:

- (a) any judgement of the High Court delivered—
 - (i) in an appeal made under Section 35G; or
 - (ii) on a reference made under Section 35G by the Appellate Tribunal before the 1st day of July, 2003;
 - (iii) on a reference made under Section 35H, in any case which, on its own motion or on an oral application made by or on behalf of the party aggrieved, immediately after passing of the judgement, the High Court certifies to be a fit one for appeal to the Supreme Court; or
- (b) on an order passed by CESTAT relating to rate of duty/valuation of goods;
- (c) by special leave petition under Article 136 of the Constitution.

Normally, the Supreme Court will entertain appeal only if—

- (a) a substantial question of law is involved;*
- (b) a question of general importance is involved;*
- (c) when manifest injustice is done;*
- (d) there are conflicting observations of the Supreme Court on same issue;*
- (e) no authoritative ruling of Supreme Court in the issue.*

Appeal will not be entertained if the Tribunal has acted bona fide with a speaking order and has considered all relevant factors even if another view may be possible.

Our Constitution has maintained a balance between powers of Legislature, Judiciary and Executive. All actions of Government are subject to judicial scrutiny of Supreme Court and High Court, irrespective of any particular statute. These judicial powers are conferred by the Constitution itself and hence cannot be curtailed by any legislation. Declaration in any statute that the order is final does not affect Writ

jurisdiction. Powers to issue high prerogative writs are extraordinary discretionary powers and hence are to be exercised sparingly and in a fit case, on sound principles of law. Court will invoke writ jurisdiction only in exceptional cases. Thus, when alternative remedy like departmental appeal or ordinary civil suit is available, writ jurisdiction will not be normally invoked.

Note: *Comparison of provisions: A statement bringing out the parallel provisions on Excise and Customs statutes pertaining to each component of the appellate scheme is appended.*

6.21.5 Powers of Committee of Chief Commissioners of Central Excise or Commissioner of Central Excise to pass certain orders on its own (Section 35E)

(1) The Committee of Chief Commissioners of Central Excise may, of its own motion, call for and examine the record of any proceeding in which a Commissioner of Central Excise as an adjudicating authority has passed any decision or order under this Act for the purpose of satisfying itself as to the legality or propriety of any such decision or order and may, by order, direct such Commissioner or any other Commissioner to apply to the Appellate Tribunal for the determination of such points arising out of the decision or order as may be specified by the Committee in its order:

Provided that where the Committee of Chief Commissioners of Central Excise differs in its opinion as to the legality or propriety of the decision or order of the Commissioner of Central Excise, it shall state the point or points on which it differs and make a reference to the Board. After considering the facts of the decision or order, if the Board considers that the decision or order passed by the Commissioner of Central Excise is not legal or proper, and then it may, direct such Commissioner or any other Commissioner to apply to the Appellate Tribunal for the determination of such points.

(2) Similarly, the Commissioner of Central Excise may, of his own motion, call for and examine any proceeding in which the order been issued by adjudicating authority subordinate to him and direct such authority or any Central Excise Officer subordinate to him to make an appeal to the Commissioner (Appeals) for the determination of such points arising out of the decision or order.

(3) **Time limit:** The Committee of Chief Commissioners of Central Excise or the Commissioner of Central Excise, as the case may be, shall make order under sub-section (1) or sub-section (2) within a period of three months from the date of communication of the decision or order of the adjudicating authority.

6.21.6 Deposit, pending appeal, of duty demanded or penalty levied (Section 35F)

Where in any appeal, the decision or order appealed against relates to any duty demanded in respect of goods which are not under the control of Central Excise authorities or any penalty levied under this Act, the person desirous of appealing against such decision or order shall, pending the appeal, deposit with the adjudicating authority the **duty demanded** or the penalty levied :

Provided that where in any particular case, the Commissioner (Appeals) or the Appellate Tribunal is of opinion that the deposit of duty demanded or penalty levied would

cause undue hardship to such person, the Commissioner (Appeals) or, as the case may be, the Appellate Tribunal, may dispense with such deposit subject to such conditions as he or it may deem fit to impose so as to safeguard the interests of revenue.

Provided further that where an application is filed before the Commissioner (Appeals) for dispensing with the deposit of duty demanded or penalty levied under the first proviso, the Commissioner (Appeals) shall, where it is possible to do so, decide such application within thirty days from the date of its filing.

Explanation: For the purposes of this section “duty demanded” shall include;

- (i) Amount determined under section 11D;
- (ii) Amount of erroneous Cenvat credit taken;
- (iii) Amount payable under rule 57CC of Central Excise Rules, 1944;
- (iv) Amount payable under rule 6 of Cenvat Credit Rules, 2001 or Cenvat Credit Rules, 2002 or Cenvat Credit Rules, 2004;
- (v) Interest payable under the provisions of this Act or the rules made there under.

6.21.7 Interest on delayed refund of amount deposited under the proviso to Section 35F (Section 35FF)

Where an amount deposited by the appellant under the first proviso to section 35F, is required to be refunded consequent upon the order of the appellate authority and such amount is not refunded within three months from the date of communication of such order to the adjudicating authority, unless the operation of the order of the appellate authority is stayed by a superior court or tribunal, there shall be paid to the appellant interest at the rate specified in section 11BB after the expiry of three months from the date of communication of the order of the appellate authority, till the date of refund of such amount.

6.21.8 Revisionary Role of The Central Government [Section 35EE]

Before the Tribunal was set up, the Central Government in the Ministry of Finance (Department of Revenue) exercised revisionary functions in regard to all cases decided at appeal level within the Department, including the Board. Even after the Tribunal was set up, the revisionary role continues, but within a drastically reduced area of operation. In Central Excise, if the Appellate orders are passed by Commissioner (Appeals) in cases of (a) loss of goods, (b) rebate of duty of excise on goods exported; or (c) export under bond without payment of duty, a Revision Application can be filed before the Central Government (Section 35-EE). However, the Central Government has the discretion to refuse such application where the amount of duty, fine or penalty determined does not exceed five thousand rupees. As would be observed, the original orders in those cases would have been passed by officers below the rank of Commissioner, since only in such case, appeals will be decided by Commissioner (Appeals). Where the Commissioner of Central Excise is of the opinion that an order passed by Commissioner (Appeals) under Section 35A is not legal or proper, he may direct the proper officer to make an application on his behalf to the Central Government for revision of such an order [Section 35EE(1A)]. If the Commissioner himself is the original authority there is no role for the Central Government as a revisionary authority.

In cases as noted above, the Revision Application against the appellate order

must be filed within three months from the date of receipt of the appellate order. The period is extendable by the Central Government (on sufficient cause being shown) by a further three months. A fee of ₹ 200/- (Rupees Two Hundred) where the amount of duty and interest demanded, fine or penalty levied by any Central Excise Officer is rupees one lakh or less and one thousand rupees in case it exceeds one lakh rupees is payable in regard to every Revision Application, and payment should be by crossed cheque to accompany the Revision Application. The applicant should also send a copy of the appellate order contested. The prescribed form for filing the Revision Application is E.A. (8). However, no fee is payable where an application is made to the Central Government for revision of an order passed by the Commissioner (Appeals) under Sub-section (1A) of Section 35EE.

On receipt of the Revision Application, it will be examined in the Ministry of Finance, after obtaining the relevant departmental records. Personal hearing, if asked for, will be granted. Decision will be taken at the level of Joint Secretary to the Government of India. As revisionary authority the Central Government also has powers to increase the penalty or demand duty or increase confiscation. However, no such action can be taken without putting the party to notice, and giving him due opportunity for defence. In case the notice is for demanding duty, the time limit of Section 11-A (one year/5 years) will apply.

6.22 SETTLEMENT COMMISSION [Section 31, 32, 32A to 32P Excise Act and Sections 127A to 127N of Customs Act]

Introduction

The disputes under excise and customs are sought to be settled by the commission expeditiously without much strain. The provisions were introduced in the Finance Act, 1998. Under this, cases are settled by the commission at the instance of the assessee who wants to accept liability without contesting the case.

Constitution and Composition of Settlement Commission

The Central Government has constituted the customs and Central Excise Settlement Commission under Section 32 of the Central Excise Act. The commission has principal Bench at Delhi and additional Benches at other three major metros. The principal Bench is headed by the chairman and the others by the vice-chairman. Two other members will be assisting them at each bench.

The commission provides quick and easy settlement of tax disputes involving high revenue stake. The purpose is to save time and energy of both the tax payer and the Department. The procedure followed by the commission is much less costly and is beneficial to the assessee.

6.22.1 Powers of the Commission

The commission will exercise its powers for settling the cases as a bench consisting of three members, and all decisions will be by majority. The Chairman has the power to constitute a large bench or special bench, wherever necessary. The commission has power to regulate its own procedures and procedures of its benches.

The commission has power to have exclusive jurisdiction to exercise the powers and perform the functions of any officer of customs/excise.

The commission can grant immunity from prosecution for any offence under Central Excise Act/Customs Act. It can also withdraw the immunity granted if the conditions specified under its order are not complied with.

The commission has power to grant waiver either wholly or in part from imposition of any penalty, fine, but NOT interest under excise/customs in respect of the case covered under the settlement.

It can order provisional attachment of property belonging to the applicant if found necessary to protect the interests of the revenue.

Note: The order of the Commission is conclusive and cannot be re-opened in any proceedings under the Acts.

6.22.2 Application to the Commission

The following categories of people fulfilling the requirements can make an application for settlement commission:

- An importer/exporter or a manufacturer can approach the settlement commission by filing an application in the prescribed form. It may be noted that the department cannot approach the commission for settlement.
- The application can only be made to admit the liability, not to contest it. The admitted liability shall be more than ₹ 3,00,000.
- The applicant can file an application in the following cases:
 - Admission of short levy on account of misclassification.
 - Under valuation.
 - Inapplicability of exemption notification/CENVAT credit.

Note: Application can not be made in case where no return has been filed.

The applicant has to deposit the additional duty with interest along with the application.

An application has only one opportunity to avail the settlement in his lifetime.

The exporter under DEEC, EOU/EPZ can approach the commission if he failed to fulfill his export obligation for reasons beyond his control.

Even an SSI units can approach the commission.

The cases involving the valuation dispute can be taken up with the commission.

Cases relating to interpretation of law and notifications can be taken up.

Persons involved in the following cases cannot approach the commission for settlement:

- *Cases involving narcotic drugs and psychotropic substances under Narcotic Drugs and Psychotropic Substances Act, 1985.*
- *Cases where the revenue has invoked the provisions of Section 123 of the Customs Act (seizure of smuggled goods and burden of proof).*
- *Cases involving interpretation of classification of goods under the Customs Tariff Act or CETA.*
- *Cases pending before the Tribunal/Court.*
- *Cases remanded by the tribunal for fresh adjudication.*

6.22.3 Procedure

- The application is to be submitted to the commission in the prescribed form with the fee and the commission will issue a dated acknowledgement immediately.
- A report is called for from the department which the department is supposed to submit within one month of receiving the communication.
- Intimation of hearing shall be issued within 2 months of receiving application.
- The proceedings will be in camera (personal, not in public).
- Only after admitting the case, the commission will open the sealed cover submitted by the applicant containing the incriminating information.
- Thereafter, the sealed cover is sent to the verification of the department. On receiving the report from the department it will proceed to decide the matter and the applicant has to deposit the amount within 30 days of order of the commission.

6.23 Powers and Duties of Officers:

(a) Power of search and seizure (Section 12F)

Where the Joint commissioner of Central Excise or Additional Commissioner of Central Excise or such other Central Excise Officer as may be notified by the Board has reasons to believe that any goods liable to confiscation or any documents or books or things which in his opinion shall be useful for or relevant to any proceedings under this Act, are secreted in any place, he may authorise in writing any Central Excise Officer to search and seize or may himself search and seize such documents or books or things.

The provisions of the Code of Criminal Procedure, 1973 relating to search and seizure shall, so far as may be, apply to search and seizure under this section subject to the modification that subsection (5) of section 165 of the said Code shall have effect as if for the word "Magistrate", wherever it occurs, the words "Commissioner of Central Excise" were substituted.

(b) Power to Arrest (Section 13)

(1) If an officer of Central Excise empowered in this behalf by general or special order of the Commissioner of Central Excise has reason to believe that any person has committed an offence punishable under this Act, he may arrest such person and shall, as soon as may be, inform him of the grounds for such arrest.

(2) Every person arrested under sub-section (1) for an offence shall, without unnecessary delay, be taken to a Magistrate.

(3) Where an officer of Central Excise has arrested any person under subsection (1), for any offence (other than an offence punishable for a term of imprisonment of three years or more under section 9), he shall, for the purpose of releasing such person on bail or otherwise, have the same powers and be subject to the same provisions as the officer-in-charge of a police station has, and is subject to, under the Code of Criminal Procedure, 1973.

(4) Notwithstanding anything contained in the Code of Criminal Procedure, 1973, all offences under this Act (except an offence punishable for a term of imprisonment of three years or more under section 9) shall be liable.

(5) Notwithstanding anything contained in the Code of Criminal Procedure, 1973, all offences punishable for a term of imprisonment of three years or more under section 9 shall be cognizable.

(c) Bail for offence punishable for a term of imprisonment of three years or more under section 9 not to be granted without hearing public prosecutor (Section 13A)

(1) Notwithstanding anything contained in the Code of Criminal Procedure, 1973, no person Accused of an offence punishable for a term of imprisonment of three years or more under section 9 shall be released on bail or on his own bond unless—

- (i) the public prosecutor has been given an opportunity to oppose the application for such release; and
- (ii) where the public prosecutor opposes the application, the Magistrate is satisfied that there are reasonable grounds for believing that he is not guilty of such offence and that he is not likely to commit any offence while on bail:

Provided that a person who is under the age of eighteen years or is a woman or is sick or infirm, may be released on bail if the Magistrate so directs.

(2) Notwithstanding anything contained in the Code of Criminal Procedure, 1973, no police officer shall, save as otherwise provided under this Act, investigate into an offence under this Act unless specifically authorised by the Central Government by a general or special order, and subject to such conditions as may be specified in the order.

(d) Searches and arrests how to be made (Section 18)

All searches under this Act or the rules made there under and all arrests under this Act shall, save as otherwise provided under this Act, be carried out in accordance with the provisions of the Code of Criminal Procedure, 1973, relating respectively to searches and arrests under that Code.

Central Excise Rules, 2002 deals with various matters relating to access to registered premises, power to stop, search etc. by authorised officials of the Central Excise Department. These powers are very essential in that the departmental officials would like to have close surveillance and vigilance over the assessee as to what he is doing at the factory wherein any excisable goods are manufactured; whether the assessee maintains proper records, whether the assessee follows prescribed procedures etc., all in an attempt to safeguard the interests of revenue. These powers assume all the more importance in view of the fact that now the self-removal procedure (SRP) stands extended to all the excisable goods. SRP is a manifestation of the Department's faith in the assessee and the assessee has the freedom to remove the goods without the requirement of the presence of an excise official at the time of each clearance of the excisable goods from the factory. Naturally, when the assessee is being trusted to that extent, the Departmental officers should also have powers to enter the premises with a view of finding out

whether the benefit given to the assessee is being in any manner put to misuse or the assessee is indulging in any other practices with a result the duty due to the Department is being evaded.

Rules 22 to 30 of the Central Excise Rules, 2002 deal with entire gamut of access, search, seizure, confiscation and penalty. These rules are self-explanatory. They are reproduced hereinbelow:

6.23.1 Access to a registered premises (Rule 22)

- (1) An officer empowered by the Commissioner in this behalf shall have access to any premises registered under these rules for the purpose of carrying out any scrutiny, verification and checks as may be necessary to safeguard the interest of revenue.
- (2) Every assessee shall furnish to the officer empowered under Sub-rule (1), a list in duplicate, of all the records prepared or maintained by the assessee for accounting of transactions in regard to receipt, purchase, manufacture, storage, sales or delivery of the goods including inputs and capital goods.
- (3) Every assessee shall, on demand makes available to the officer empowered under Sub-rule (1) or the audit party deputed by the Commissioner or the Comptroller and Audit General of India:
 - (i) the records maintained or prepared by him in terms of Sub-rule (2);
 - (ii) the cost audit reports, if any, under Section 233B of the Companies Act, 1956 (1 of 1956); and
 - (iii) the Income-tax audit report, if any under Section 44AB of Income-tax Act, 1961 (43 of 1961),

for the scrutiny of the officer or audit party, as the case may be.

6.23.2 Power to stop and search (Rule 23)

Any Central Excise Officer, may search any conveyance carrying excisable goods in respect of which he has reason to believe that the goods are being carried with the intention of evading duty.

6.23.3 Return of records (Rule 24A)

The books of accounts or other documents, seized by the Central Excise Officer or produced by an assessee or an other person, which have not been relied on for the issue of notice under the Act or the rules made thereunder, shall be returned within thirty days of the issue of said notice or within 30 days from the date of expiry of the period for issue of said notice:

Provided that the commissioner of Central Excise may order for the retention of such books of accounts or documents for reasons to be recorded in writing and the Central Excise Officer shall intimate to the assessee or such person about such retention.

6.23.4 Power to detain goods or seize the goods (Rule 24)

If a Central Excise Officer, has reason to believe that any goods, which are liable to excise duty but no duty has been paid thereon or the said goods were removed

with the intention of evading the duty payable thereon, the Central Excise Officer may detain or seize such goods.

6.23.5 Confiscation and penalty (Rule 25)

Subject to the provisions of Section 11 AC of the Act, if any producer, manufacturer, registered person of a warehouse or a registered dealer:

- (a) removes any excisable goods in contravention of any of the provisions of these rules or the notifications issued under these rules; or
- (b) does not account for any excisable goods produced or manufactured or stored by him; or
- (c) engages in the manufacture, production or storage of any excisable goods without having applied for the registration certificate required under Section 6 of the Act; or
- (d) contravenes any of the provisions of these rules or the notifications issued under these rules with intent to evade payment of duty,—

then, all such goods, shall be liable to confiscation and the producer or manufacturer or registered person of the warehouse or a registered dealer, as the case may be, shall be liable to a penalty not exceeding the duty on the excisable goods in respect of which any contravention of the nature referred to in clause (a) or clause (b) or clause (c) or clause (d) has been committed, or rupees two thousand, whichever is greater.

(2) An Order under Sub-rule (1) shall be issued by the Central Excise Officer, following the principles of natural justice.

6.23.6 Penalty for certain offences (Rule 26)

Any person who acquires possession of, or is in any way concerned in transporting, removing, depositing, keeping, concealing, selling or purchasing or in any other manner deals with any excisable goods which he knows or has reason to believe are liable to confiscation under the Act or these rules, shall be liable to a penalty not exceeding the duty on such goods or rupees two thousand, whichever is greater.

(2) Penal action against the person is taken who issues CENVAT Invoice without of goods mentioned therein.

Action is also taken against the person who fabricates any central excise or customs duty falsely conferring any benefit such as CENVAT credit, refund etc.

A breach of these rules shall, where no other penalty is provided herein or in the Act, be punishable with a penalty which may extend to five thousand rupees and with confiscation of the goods in respect of which the offence is committed. (Rule 27)

6.23.7 On confiscation, property to vest in the Central Government (Rule 28)

- (1) When any goods are confiscated under these rules, such thing shall thereupon vest in the Central Government.
- (2) The Central Excise Officer adjudging confiscation shall take and hold possession of the things confiscated, and every Officer of Police on the

requisition of such Central Excise Officer, shall assist him in taking and holding such possession.

6.23.8 Disposal of goods confiscated (Rule 29)

Goods of which confiscation has been adjudged and in respect of which the option of paying a fine in lieu of confiscation has not been exercised, shall be sold, destroyed or otherwise disposed of in such manner as the Commissioner may direct.

6.23.9 Storage charges in respect of goods confiscated and redeemed (Rule 30)

If the owner of the goods, the confiscation of which has been adjudged, exercises his option to pay fine in lieu of confiscation he may be required to pay such storage charges as may be determined by the adjudicating officer.

6.24 Power of Adjudication

Sections 33 to 34A of the Central Excise Act, 1944 deals with adjudication of confiscations and penalties. These sections provides for powers of adjudication to Officers of Central Excise where anything is liable to confiscation or any person is liable to penalty under the Act, along with giving them the option to pay fine in lieu of confiscation etc. These sections are reproduced below:

Where under this Act or by rules made thereunder anything is liable to confiscation or any person is liable to penalty, such confiscation or penalty may be adjusted:

- (a) without limit by a Commissioner of Central Excise;
- (b) upto confiscation of goods not exceeding five hundred rupees in value and imposition of penalty not exceeding two hundred and fifty rupees by an Assistant Commissioner of Central Excise.

Provided that the Central Board of Excise and Customs constituted under the Central Board of Revenues Act, 1963, may in the case of any officer performing the duties of an Assistant Commissioner of Central Excise, reduce the limits indicated in clause (b) of this section and may confer on any officer of the powers indicated in clause (a) of this section.

Section 33A has been inserted by the Finance (No. 2) Act, 2004 providing for adjudication procedure. As per this Section, an adjudicating authority provides an opportunity of being heard to a party in a proceeding, if the party so desires. Such authority may grant time, from time to time, to the parties or any of them and adjourn the hearing for reasons to be recorded in writing. However, no such adjournment shall be granted more than three times to a party during the proceeding.

6.24.1 Option to pay fine in lieu of Confiscation (Section 34)

Whenever confiscation is adjudged under this Act or the rules made thereunder, the Officer adjudging it, shall give the owner of the goods an option to pay fine in lieu of confiscation, such fine as the officer thinks fit.

6.24.2 Confiscation and penalty not to interfere with other punishments (Section 34A)

No confiscation made or penalty imposed under the provisions of the Act or of any rules made thereunder shall prevent infliction of any other punishment to which the person affected thereby is liable, under the provisions of this Act or under any other law.

6.25 Procedure to be followed in cases where duty is paid under protest

Where an assessee desires to pay duty under protest he shall deliver to the Proper Officer a letter to this effect and give grounds for payment of the duty under protest. On receipt of the said letter, the Proper Officer shall give an acknowledgement to it.

The acknowledgement so given shall, subject to the provisions of Sub-rule (4), be the proof that the assessee has paid the duty under protest from the day on which the letter of protest was delivered to the Proper Officer. An endorsement "Duty paid under protest" shall be made on all copies of the invoice, the Application for Removal and form ER-I / ER-II, as the case may be.

In cases where the remedy of an appeal or revision is not available to the assessee against an order or decision which necessitated him to deposit the duty under protest, he may, within three months of the date of delivery of the letter of protest give a detailed representation to the Assistant/Deputy Commissioner of Central Excise.

In cases where the remedy of an appeal or revision is available to the assessee against an order or decision which necessitated him to deposit the duty under protest, he may file an appeal or revision within the period specified for filing such appeal or revision, as the case may be.

On service of the decision on the representation referred to in Sub-rule (5) or of the appeal or revision referred to in Sub-rule (6) the assessee shall have no right to deposit the duty under protest:

Provided that an assessee shall be allowed to deposit the duty under protest during the period available to him for filing an appeal or revision, as the case may be, and during the pendency of such appeal or revision, as the case may be.

If any of the provisions of this rule has not been observed, it shall be deemed that the assessee has paid the duty without protest.

Note: A letter of protest or a representation shall not constitute a claim for refund.

6.26 Special audit in certain cases (Section 14A)

(1) If at any stage of enquiry, investigation or any other proceedings before him, any Central Excise Officer not below the rank of an Assistant Commissioner of Central Excise, or Deputy Commissioner of Central Excise having regard to the nature and complexity of the case and the interest of revenue, is of the opinion that the value has not been correctly declared or determined by a manufacturer or any person, he may, with the previous approval of the Chief Commissioner of Central Excise, direct such manufacturer or such person to get the accounts of his factory, office, depots, distributors or any other place, as may be specified by the said Central

Excise Officer, audited by a cost accountant or Chartered accountant, nominated by the Chief Commissioner of Central Excise in this behalf.

(2) The cost accountant or Chartered accountant, so nominated shall, within the period specified by the Central Excise Officer, submit a report of such audit duly signed and certified by him to the said Central Excise Officer mentioning therein such other particulars as may be specified:

Provided that the Central Excise Officer may, on an application made to him in this behalf by the manufacturer or the person and for any material and sufficient reason, extend the said period by such further period or periods as he thinks fit; so, however, that the aggregate of the period originally fixed and the period or periods so extended shall not, in any case, exceed one hundred and eighty days from the date on which the direction under sub-section (1) is received by the manufacturer or the person.

(3) The provisions of sub-section (1) shall have effect notwithstanding that the accounts of the manufacturer or person aforesaid have been audited under any other law for the time being in force or otherwise.

(4) The manufacturer or the person shall be given an opportunity of being heard in respect of any material gathered on the basis of audit under sub-section (1) and proposed to be utilised in any proceedings under this Act or rules made thereunder.

Explanation 1- For the purpose of this section, "cost accountant" shall have the meaning assigned to it in clause (b) of sub-section (1) of Section 2 of the Cost and Works Accountants Act, 1959 (23 of 1959).

Explanation 2 – For the purpose of this section, "chartered accountant" shall have the meaning assigned to it in clause (b) of sub-section (1) of Section 2 of the Chartered Accountants Act, 1949 (38 of 1949).

6.27 Special audit in cases where credit of duty availed or utilized is not within the normal limits, etc. (Section 14AA)

(1) If the Commissioner of Central Excise has reason to believe that the credit of duty availed of or utilised under the rules made under this Act by a manufacturer of any excisable goods -

- (a) is not within the normal limits having regard to the nature of the excisable goods produced or manufactured, the type of inputs used and other relevant factors, as he may deem appropriate;
- (b) has been availed of or utilised by reason of fraud, collusion or any willful mis-statement or suppression of facts, he may direct such manufacturer to get the accounts of his factory, office, depot, distributor or any other place, as may be specified by him, audited by a cost accountant or Chartered accountant nominated by him.

(2) The cost accountant or Chartered accountant so nominated shall, within the period specified by the Commissioner of Central Excise, submit a report of such audit duly signed and certified by him to the said Commissioner mentioning therein such other particulars as may be specified.

(3) The provisions of sub-section (1) shall have effect notwithstanding that the accounts of the said manufacturer aforesaid have been audited under any other law for the time being in force or otherwise.

(4) The manufacturer shall be given an opportunity of being heard in respect of any material gathered on the basis of the audit under sub-section (1) and proposed to be utilised in any proceeding under this Act or rules made thereunder.

Explanation - 1 For the purpose of this section, “cost accountant” shall have the meaning assigned to it in clause (b) of sub-section (1) of section 2 of the Cost and Works Accountants Act, 1959 (23 of 1959).]

Explanation - 2 For the purpose of this section, “chartered accountant” shall have the meaning assigned to it in clause (b) of sub-section (1) of Section 2 of the Chartered Accountants Act, 1949 (38 of 1949).

6.28 CENVAT Credit Rules, 2004

Definitions

(a) “**Capital goods**” means:

(A) the following goods, namely:

- (i) all goods falling under Chapter 82, Chapter 84, Chapter 85, Chapter 90, heading No. 68.04 and sub-heading No. 6805.10 of the First Schedule to the Excise Tariff Act;
- (ii) pollution control equipment;
- (iii) components, spares and accessories of the goods specified at (i) and (ii) above;
- (iv) moulds and dies, jigs and fixtures;
- (v) refractories and refractory materials;
- (vi) tubes and pipes and fittings thereof; and
- (vii) storage tank; and
- (viii) motor vehicles other than those falling under tariff headings 8702, 8703, 8704, 8711 and their chassis, but including dumpers and tippers used—
 - (1) in the factory of the manufacturer of the final products, but does not include any equipment or appliance used in an office; or
 - (1A) outside the factory of the manufacturer of the final products for generation of electricity for captive use within the factory or
 - (2) for providing output service;
- (B) motor vehicle designed for transportation of goods including their chassis registered in the name of the service provider, when used for—
 - (i) providing an output service of renting of such motor vehicle; or

- (ii) transportation of inputs and capital goods used for providing an output service; or
 - (iii) providing an output service of courier agency”
 - (C) motor vehicle designed to carry passengers including their chassis, registered in the name of the provider of service, when used for providing output service of-
 - (i) transportation of passengers; or
 - (ii) renting of such motor vehicle; or
 - (iii) imparting motor driving skills”
 - (D) components, spares and accessories of motor vehicles which are capital goods for the assessee;
- (b) **“Exempted Goods”** means excisable goods which are exempt from the whole of the duty of excise leviable thereon, and includes goods which are chargeable to “Nil” rate of duty and goods in respect of which the benefit of an exemption under notification No. 1/2011 CE dated the 1st March 2011 is availed;
- (c) **“Exempted Services”** means a—
- (1) taxable service which is exempt from the whole of the service tax leviable thereon; or
 - (2) service, on which no service tax is leviable under section 66B of the Finance Act; or
 - (3) taxable service whose part of value is exempted on the condition that no credit of inputs and input services, used for providing such taxable service, shall be taken; but shall not include a service which is exported in terms of rule 6A of the Service Tax Rules, 1994.’
- (d) **“Finance Act”** means the Finance Act, 1994 (32 of 1994);
- (e) **“Final Products”** means excisable goods manufactured or produced from input, or used input service;
- (f) **“First Stage Dealer”** means a dealer, who purchases the goods directly from,—
- (i) the manufacturer under the cover of an invoice issued in terms of the provisions of Central Excise Rules, 2002 or from the depot of the said manufacturer, or from premises of the consignment agent of the said manufacturer or from any other premises from where the goods are sold by or on behalf of the said manufacturer, under cover of an invoice; or
 - (ii) an importer or from the depot of an importer or from the premises of the consignment agent of the importer, under cover of an invoice;
- (g) **“input”** means—
- (i) all goods used in the factory by the manufacturer of the final product; or
 - (ii)(a) any goods including accessories, cleared along with the final

product, the value of which is included in the value of the final product; and

(b) goods used for providing free warranty for final product; or

“**Free Warranty**” means a warranty provided by the manufacturer –

- the value of which is included in the price of the final products and
- is not charged separately from the customer.

(iii) all goods used for generation of electricity or steam for captive use; or

(iv) all goods used for providing any output service but excludes –

(A) Light diesel oil, high speed diesel oil or motor spirit commonly known as petrol;

(B) Any goods used for -

(a) construction or execution of works contract of a building or a civil structure or a part thereof; or

(b) laying of foundation or making of structures for support of capital goods, except for the provision of service portion in the execution of a works contract or onstruction service as listed under clause (b) of section 66E of the Act;

(C) Capital goods except when used as parts or components in the manufacture of a final product;

(D) Motor Vehicles;

(E) (i) any goods, such as food items

(ii) goods used in a guesthouse, residential colony, club or a recreation facility and clinical establishment, when such goods are used primarily for personal use or consumption of any employee; and

(F) any goods which have no relationship whatsoever with the manufacture of a final product.

(h) **Input Services** means any service,

- used by a provider of output service for providing an output service; or
- used by the manufacturer, whether directly or indirectly, in or in relation to the manufacture of final products and clearance of final products upto the place of removal,

and includes services used in relation to setting up, modernization, renovation or repairs of a factory, premises of provider of output service or an office relating to such factory or premises, advertisement or sales promotion, market research, storage upto the place of removal, procurement of inputs, activities relating to business, such as accounting, auditing, financing, recruitment and quality control, coaching and training, computer networking, credit rating, share registry, and security, inward transportation of inputs or capital goods and outward transportation upto the

place of removal but excludes

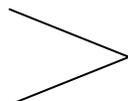
- (A) service portion in the execution of a works contract and construction services including service listed under clause (b) of section 66E of the Finance Act (hereinafter referred as specified services) in so far as they are used for -
 - (a) construction or execution of works thereof; or contract of a building or a civil structure or a part;
 - (b) laying of foundation or making of structures for support of capital goods, except for the provision of one or more of the specified services; or;
- (B) services provided by way of renting of a motor vehicle in so far as they relate to a motor vehicle which is not a capital goods or
- (BA) service of a general insurance business, servicing, repair and maintenance, in so far as they relate to a motor vehicle which is not a capital goods, except when used by –
 - (a) a manufacturer of a motor vehicle in respect of a motor vehicle manufactures by such person; or
 - (b) an insurance company in respect of a motor vehicle insured or reinsured by such person or.
- (C) such as those provided in relation to outdoor catering, beauty treatment, health and fitness centre, life insurance, health insurance and travel benefits extended to employees on vacation such as Leave or Home Travel Concession, when such services are used primarily for personal or consumption of any employee.
- (i) **“input service distributor”** means an office of the manufacturer or producer of final products or provider of output service, which receives invoices issued under rule 4A of the Service Tax Rules, 1994 towards purchases of input services and issues invoice, bill or, as the case may be, challan for the purpose of distributing the credit of service tax paid on the said services to such manufacturer or producer or provider, as the case may be;
- (j) **“job work”** means processing or working upon of raw material or semi-finished goods supplied to the job worker, so as to complete a part or whole of the process resulting in the manufacture or finishing of an article or any operation which is essential for aforesaid process and the expression “job worker” shall be construed accordingly;
- (k) **Output Services**
Output service means any service provided by a provider of service located in the taxable territory but shall not include a service,-
 - (1) specified in section 66D of the Finance Act; or
 - (2) where the whole of service tax is liable to be paid by the recipient of service.
- (l) **“second stage dealer”** means a dealer who purchases the goods from a first stage dealer.

Substantive Provisions

- *The Cenvat Credit Scheme is a beneficial set off scheme.*
- *It aims at eliminating/reducing cascading effect of taxes.*
- *This scheme is available to both service providers and manufacturers.*
- *Under this, excise duties and service tax including education cess paid on inputs, capital goods and input services are available as credit. [Rule 3(1)]*
- *Such credit can be utilized against the excise duties and service tax (including education cess) payable on final products and output services. [Rule 3(4) & 3(7)(b)]*
- *All important terms such as capital goods, input, input service, final product, output service have been defined under the Cenvat Credit Rules, 2004. [Rule 2(a); (k); (l)]*
- *Documents and records needed and the procedure to be followed have been specified under the rules. [Rule 9]*
- *Penalties for specific violations have been provided. [Rules 14 & 15]*
- *General penalty also has been provided. [Rule 15A]*
- *The mechanism of Credit transfer through Input Service Distributor and output service provider has been facilitated. [Rule 7 & 7A]*
- *The Rules also provide for refund of Cenvat Credit in special cases. [Rules 5 & 5A]*
- *Transfer of credit in case of merger, amalgamation and shifting of factory has been provided the rules. [Rule 10]*

Taking and utilizing of Cenvat Credit is subject to

Eligibility,
Conditions &
Limitations



as specified under the Rules

Eligibility

Persons: manufacturer of excisable goods and provider of taxable services.

Items: Inputs; capital goods and input services.

Conditions for availing CENVAT CREDIT, Refund of Cenvat Credit:

Rule 3 (1): Duties/taxes in respect of which CENVAT credit is allowed:

- (a) Basic Excise duty (BED), however, the Cenvat credit of such duty shall not be allowed to be taken when paid on any goods in respect of which the benefit of exemption under Notification No.1/2011CE dated 1st March 2011 is availed or specified in serial numbers 67 and 128 in respect of which the benefit of an exemption under Notification No.12/2012 dated 17th March 2012 is availed
- (b) Special Duty of Excise (SED);
- (c) Additional duty of excise leviable under section 3 of Additional duty of excise (textile and textile article) Act, 1978 [AED (T&TA)];

- (d) Additional duty of excise under section 3 of Additional duty of excise (goods of special importance) Act, 1957. (GSI);
- (e) National Calamity Contingent Duty (NCC);
- (f) Education cess and Secondary & Higher education cess (SHEC);
- (g) Additional duty of customs (ADC) equivalent to duty of excise specified in (a), (b), (c), (d), (e) and (f) above;
 However, CENVAT credit shall not be allowed in excess of 85% of the additional duty of customs paid under Section 3(1) of Customs Tariff Act, on ships, boats and other floating structures for breaking up falling under tariff item 8908 00 00 of the first schedule to Customs Tariff Act.
- (h) Additional duty of customs under Section 3(5) of Customs Tariff Act (CTA);
- (i) Additional duty of excise on tea and tea waste (ADE);
- (j) Service tax, education cess and SHEC on taxable services;
- (k) Service tax leviable under section 66B of the Finance Act.
- (l) health cess;

Specific restrictions in relation to utilization of credit in respect of the duties and taxes:

- (a) BED, SED, GSI, Service tax can be utilized for payment of any duty except clean energy cess and health cess;
- (b) AED(T&TA) can be utilized only AED (T&TA)
- (c) National calamity contingent duty can be utilized only towards National calamity contingent duty;
- (d) ADE can be utilized towards ADE only;
- (e) ADC under Section 3(5) of CTA can be utilized for all duties except service tax and health cess;
- (f) Education cess and SHEC on excise and service tax can be utilized against education cess and SHEC on excise and service tax;
- (g) No credit of clean energy cess is available under Rule 3(1);
- (h) Health cess can be utilized against Health cess only;
- (i) CENVAT credit of any of the duties specified in Rule 3(1) shall not be utilized for payment of excise duty on any goods in respect of which exemption under Notification No. 1/2011 dated 01/03/2011 is availed.

Rule 3(2): When the exempted final products became dutiable, the manufacturer is entitled to take credit on inventory lying with him.

Inventory may consist of inputs lying as stock, inputs contained in the semi-finished goods and finished goods which are lying in stock with the manufacturer.

Exempted goods means goods fully exempted and includes goods chargeable to nil rate.

Rule 3(3): Input service provider is also entitled to take credit on inventory with him when his services became taxable.

Exempted services means services fully exempt and includes services on which no service tax is leviable.

Application and Quantum of Cenvat Credit

Rule 3(4): Utilisation of Cenvat Credit: Cenvat Credit may be utilized for payment of

- (a) any duty of excise on any final product

Payment of any duty on any final product indicates that matching is not required between input and output. It means that one on one correlation is not necessary. But it is subject to matching of duties under Rule 3(7)(b).

But the above facility is not available to units in North East region, Kutch District of Gujarat etc. which enjoy special benefit of refund of duty under Rule 12.

- (b) amount payable on inputs removed as such or as partially processed;

- (c) amount payable on capital goods removed as such;

the amount payable by utilizing the Cenvat credit under (b) and (c) above is same as [equivalent to] the amount of credit taken on them.

- (d) amount payable on repaired/reconditioned goods when they are sent back after such repair/reconditioning under Rule 16(2) of Central Excise Rules.

- (e) service tax on any output service.

Provisos: Utilisation of credit as above is subject to the following:

1. Credit available only upto the end of the month or quarter as the case may be, is allowed to be utilized for the payment of service tax or excise duty.

Excise duty for the removals in a given month is payable monthly by 5th or 15th of the following month. So, Credit available by month end alone can be utilized for the payment of duty for the same month.

Example: Credit balance as on 31st January is ₹ 75,000, on 5th February it is ₹ 87,000.

Duty payable for January is ₹ 90,000. How much credit can the assessee utilize from the Cenvat Credit Account?

Answer: ₹ 75,000 [though the duty is payable on 5th February, the balance available up to January end only can be utilized.]

Similarly, service tax is payable quarterly by the non corporate service providers. They can utilize only the credit amount available by the end of the quarter.

2. The service provider is not eligible to take credit on special CVD paid on imported goods under Section 3(5) of the Customs Tariff Act, 1975.

3. Additional duty paid under Section 85 of the Finance Act, 2005 alone can be utilized for the additional duty payable on the final product under Section 85 of the Finance Act, 2005.

Note: Additional duty under Section 85 is payable on pan masala and tobacco products. It means health cess available as credit alone can be utilized for the payment of health cess at the output level.

4. The Cenvat Credit of any duty specified in sub-rule (1) except NCCD shall not be utilized for payment of the NCCD on mobile.

If no credit is available under Section 85, it is payable through PLA/GAR-7 challan.

Example: On 31st January, the Cenvat Credit balances are as follows:

Cenvat: ₹ 58,000; Under Section 85 of Finance Act, 2005: ₹ 4,000.

The duties payable on final products are as follows: Cenvat ₹ 35,000; Under Section 85: ₹ 7,500; NCCD ₹ 1500 on mobile.

Ans.: CENVAT balance of ₹ 58,000 can be utilized only for CENVAT; it cannot be used for paying duty under Section 85 and NCCD.

Hence the balance of ₹ 3,500 [7,500 – 4,000] plus ₹ 1500 shall be met through PLA or by direct cash deposit in the bank.

Explanation: The Cenvat credit cannot be used for payment of service tax in respect of services where the person liable to pay tax is the services recipient.

Rule 3(5): When inputs or capital goods are removed as such, the cenvat user is required to pay an amount equal to the amount taken on such inputs or capital goods.

He is also required to remove them under the cover of invoice.

If the capital goods, on which CENVAT Credit has been taken, are removed, after being used, the manufacturer or service provider shall pay an amount equal to the CENVAT Credit taken as reduced by following specified percentage on straight line method from the date of CENVAT Credit taken.

No such payment is necessary:

- if the inputs are removed outside for providing output service.
- if the capital goods removed outside for providing output service.
- If any inputs are removed outside the factory for providing free warranty for final products.

Rule 3(5A):

Prior to amendment, this rule specify for reversal of Cenvat credit taken on capital goods which are cleared as waste or scrap. But now, If the capital goods, on which CENVAT credit has been taken, are removed after being used, whether as capital goods or as scrap or waste, the manufacturer or provider of output services shall pay an amount equal to the CENVAT Credit taken on the said capital goods

reduced by the percentage points calculated by straight line method as specified below for each quarter of a year or part thereof from the date of taking the CENVAT Credit, namely:-

(a) for computers and computer peripherals :

<i>For Each Quarter</i>	<i>At the rate</i>
First year	10%
Second year	8%
Third year	5%
Fourth and fifth year	1%

(b) for capital goods, other than computers and computer peripherals @ 2.5% for each quarter.

Provided that if the amount so calculated is less than the amount equal to the duty leviable on transaction value, the amount to be paid shall be equal to the duty leviable on transaction value.

Rule 3(5B): If value of any inputs or capital goods are written off fully or partially before they are put to use, or provision has been made for writing off fully or partially, then the manufacturer or service provider is liable to pay amount equal to cenvat credit in respect of such inputs/capital goods. However, if the input or capital goods are used subsequently, the credit can be taken.

Rule 3(6): The buyer of inputs and capital goods [including scrap under Rule 3(5A)] is eligible to take Cenvat Credit on duty paid by him.

Special cases: Rule 3(7) – Exceptions to Rule 3(1) and Rule 3(4)

Rule 3(7)(a): This sub rule gives the formula for calculating the eligible amount of Cenvat Credit on purchases from EOUs, EHTPs & STPs. These units are eligible to get concession on their DTA clearances upto certain limits.

Rule 3(7)(b): This sub-rule clarifies the matching of duties to be observed while availing the Cenvat Credit.

Utilization of input level duties and taxes is subject to matching.

Except Cenvat and SED under First and Second Schedule to CETA, additional duty paid under ADE(GSI) Act and Service tax, all other duties and taxes paid on inputs, capital goods and input services shall be used only for their respective duties and taxes payable on final products.

Eg. Additional duty paid on inputs under Section 85 of Finance Act, 2005 can be utilized for payment of Additional duty payable on final products under Section 85 of Finance Act, 2005 only and not on any other duty.

NCCD paid on inputs can be used only for payment of NCCD on any final products only and not for any other duty.

Relaxations:

Education cess is interchangeable. That means, cess paid on service tax can be used for payment of cess on final products cleared and vice versa.

Additional duty of Excise paid on ADE(GSI) can be used not only for ADE(GSI), but also for payment of Cenvat and SED on final products.

Explanation: If any other Notification or legal provision provides for exemption by denying Cenvat Credit, such provision will prevail over these Rules.

Rule 4: Conditions for Availing Cenvat Credit

1. 100% of duty paid on inputs can be taken by manufacturer and service provider immediately on bringing them in the factory/premises. [Rule 4(1)]

Provided further that the CENVAT credit in respect of inputs may be taken by the provider of output service when the inputs are delivered to such provider, subject to maintenance of documentary evidence of delivery and location of the inputs.

2. There is no compulsion that the credit must be taken immediately. There is no time limit for taking credit after bringing goods. But it cannot be taken before bringing goods.
3. A maximum of 50% only is allowed as credit on capital goods received in the factory/premises of the provider of output service or out side the factory of the manufacturer of the final products for generation of electricity for captive use within the factory in the first financial year of purchase. [Rule 2(2)(a)]
4. However, 100% credit is allowed in the following cases:
 - When the capital goods are removed as such in the same financial year.
 - When additional duty of Customs under Section 3(5) of the Customs Tariff Act is paid by Manufacturer on capital goods imported.

Reminder: Service provider is not at all eligible to take credit on additional duty of Customs paid under Section 3(5) of the Customs Tariff Act.

Where 100% can not be taken and only a part of duty has been taken as credit, the remaining balance of credit can be taken in the subsequent financial year if the capital goods are still in possession.

However, possession as a condition for availing the remaining credit in the next financial year is not applicable to the following capital goods:

- components, spares and accessories,
- refractories and refractory materials,
- moulds, dies and specified goods under Chapter 68 of CETA,
- even if the above goods are NOT in possession in the subsequent financial years, balance of credit can be taken.

Comment: possession as a condition is not insisted on the above goods as they are not long lasting.

Other conditions

It is not necessary to purchase capital goods to get Cenvat credit. Credit can be taken even on those obtained by lease, hire purchase and loan arrangement. [Rule 4(3)]

- Depreciation under Section 32 of Income Tax Act, 1961 can not be claimed on the amount of duty on which Cenvat Credit has been taken. It means, double advantage of Cenvat credit as well as depreciation can not be taken. Only either of them is permitted. [Rule 4(4)]
- Inputs and capital goods are allowed to be sent for job work by taking credit on them. But the credit is forgone if the goods sent are not received back within 180 days of sending.

However, the credit can be restored when the goods are finally received back in the factory or premises.

- The manufacturer of final products can also take credit on jigs, fixtures, moulds and dies sent to job-worker. [Rule 4(5)].
- The jurisdictional AC/DC may allow the final products to be cleared from the premises of the job worker.
- Such permission by order is valid for a financial year.
- Such permission may also be subject to some conditions imposed in the interests of Revenue [Rule 4(6)]

Provided also that the CENVAT credit in respect of capital goods may be taken by the provider of output service when the capital goods are delivered to such provider, subject to maintenance of documentary evidence of delivery and location of the capital goods.

Special Condition for availing input service Credit [Rule 4(7)]

Cenvat credit in respect of input service is allowed only after payment of value of services together with service tax evidencing through documents required under these Rules.

Rule 5: Refund of Cenvat Credit

A manufacturer who clears a final product or an intermediate product for export without payment of duty under bond or letter of undertaking, or a service provider who provides an output service which is exported without payment of service tax, shall be allowed refund of CENVAT credit as determined by the following formula subject to procedure, safeguards, conditions and limitations, as may be specified by the Board by notification in the Official Gazette:

$$\text{Refund amount} = \frac{\text{Export turnover of goods} + \text{export of goods}}{\text{Total turnover}} \times \text{Net Cenvat credit}$$

Where,-

- (A) Refund amount means the maximum refund that is admissible;

- (B) Net CENVAT credit means total CENVAT credit availed on inputs and input services by the manufacturer or the output service provider reduced by the amount reversed in terms of sub-rule (5C) of rule 3, during the relevant period;
- (C) Export turnover of goods means the value of final products and intermediate products cleared during the relevant period and exported without payment of Central Excise duty under bond or letter of undertaking;
- (D) Export turnover of services means the value of the export service calculated in the following manner, namely:-
 Export turnover of services = payments received during the relevant period for export services + export services whose provision has been completed for which payment had been received in advance in any period prior to the relevant period – advances received for export services for which the provision of service has not been completed during the relevant period;
- (E) Total turnover means sum total of the value of -
- (a) all excisable goods cleared during the relevant period including exempted goods, dutiable goods and excisable goods exported;
 - (b) export turnover of services determined in terms of clause (D) of sub-rule (1) above and the value of all other services, during the relevant period; and
 - (c) all inputs removed as such under sub-rule (5) of rule 3 against an invoice, during the period for which the claim is filed.

(2) This rule shall apply to exports made on or after the 1st April, 2012:

Provided that the refund may be claimed under this rule, as existing, prior to the commencement of the CENVAT Credit (Third Amendment) Rules, 2012, within a period of one year from such commencement:

Provided further that no refund of credit shall be allowed if the manufacturer or provider of output service avails of drawback allowed under the Customs and Central Excise Duties and Service Tax Drawback Rules, 1995, or claims rebate of duty under the Central Excise Rules, 2002, in respect of such duty; or claims rebate of service tax under the Export of Services Rules, 2005 in respect of such tax.

Explanation 1.- For the purposes of this rule,-

(1) export service - means a service which is provided as per the provisions of Export of Services Rules, 2005, whether the payment is received or not;

(2) relevant period - means the period for which the claim is filed.

Explanation 2. - For the purposes of this rule, the value of services, shall be determined in the same manner as the value for the purposes of sub-rule (3) and (3A) of rule 6 is determined.

Rule 5B: Refund of CENVAT credit to service providers providing services taxed on reverse charge basis

A provider of service providing services notified under sub-section (2) of section 68 of the Finance Act and being unable to utilise the CENVAT credit availed on

inputs and input services for payment of service tax on such output services, shall be allowed refund of such unutilised CENVAT credit subject to procedure, safeguards, conditions and limitations, as may be specified by the Board by notification in the Official Gazette.

Rule 6: Obligations of a manufacturer or producer of final products and a provider of output service

Rule 6(1): CENVAT credit shall not be allowed on inputs used in or in relation to the manufacture of exempted goods or for provision of exempted services or input services used in or in relation to the manufacture of exempted goods and their clearance upto the place of removal or for provision of exempted services.

Rule 6(2): Where a manufacturer or provider of output service avails of CENVAT credit in respect of any inputs or input services and manufactures such final products or provides such output service which are chargeable to duty or tax as well as exempted goods or services, then, the manufacturer or provider of output service shall maintain separate accounts for –

- (a) the receipt, consumption and inventory of inputs used –
 - (i) in or in relation to the manufacture of exempted goods;
 - (ii) in or in relation to the manufacture of dutiable final products excluding exempted goods;
 - (iii) for the provision of exempted services;
 - (iv) for the provision of output services excluding exempted services; and
- (b) the receipt and use of input services –
 - (i) in or in relation to the manufacture of exempted goods and their clearance upto the place of removal;
 - (ii) in or in relation to the manufacture of dutiable final products, excluding exempted goods, and their clearance upto the place of removal;
 - (iii) for the provision of exempted services; and
 - (iv) for the provision of output services excluding exempted services,

and shall take CENVAT credit only on inputs under sub-clause (ii) and (iv) of clause (a) and input services under sub-clauses (ii) and (iv) of clause (b).

Rule 6(3): Where the manufacturer of goods opts for not to maintain separate account then he shall reverse the CENVAT credit attributable to exempted goods/services in the following manner:

- (i) manufacturer of goods shall pay an amount equal to 6% (this limit is increased from 5% to 6% w.e.f 1st July 2012) of value of exempted goods and the provider of output service shall pay an amount equal to 6% of the value of exempted services
- (ii) the manufacturer of goods and provider of output service shall pay an amount equivalent to the CENVAT credit as determined in sub-rule 3(A)
- (iii) the manufacturer of goods or provider of output services shall maintain separate accounts for receipt, consumption and inventory of inputs as mentioned in sub rule 2(a) and take CENVAT credit only on inputs used in

or in relation to manufacture of dutiable final products or dutiable output services and pay an amount as determined under sub-rule (3A) in respect of input services.

Provided that in case of transportation of goods or passengers by rail the amount required to be paid under clause (i) shall be an amount equal to 2 per cent of value of the exempted services.

Rule 6(3A): If the manufacturer or service provider, opts for payment of duty determined under sub-clause (ii) & (iii) of Rule 6(3) then he shall follow the procedure prescribed in this Rule.

- (i) Intimate the superintendent in writing the following
 - (a) Name, address and registration number.
 - (b) Date of exercising the option
 - (c) Description of dutiable goods or output services.
 - (d) Description of exempted goods or exempted services
 - (e) CENVAT of input and input services lying in balance on the date of exercising the option.
- (ii) The manufacturer of goods or provider of output service shall provisionally determine and pay for every month –
 - (a) Amount of CENVAT credit attributable to inputs used in or in relation to manufacture of exempted goods
 - (b) Amount of CENVAT credit on inputs used for provision of exempted services,

$$= \frac{\text{Value of exempted services provided during the preceding financial year}}{\text{Value of dutiable goods manufactured and removed + Value of output and exempted services provided during the preceding financial year}} \times \text{CENVAT credit taken on inputs during the month – CENVAT credit attributable to inputs used in or in relation to manufacture of exempted goods}$$

- (c) Amount of CENVAT credit attributable to input services used in or in relation to manufacture of exempted goods and their clearance upto the place of removal or for the provision of exempted services.

$$= \frac{\text{Value of exempted services provided + Value of exempted goods manufactured and removed during the preceding financial year}}{\text{Value of dutiable and exempted goods Manufactured and removed + Value of output and exempted services provided during the preceding financial year}} \times \text{CENVAT credit taken on inputs services during the month}$$

(iii) The manufacturer of goods or provider of output service shall finally determine the amount of CENVAT credit attributable to exempted goods and exempted services for the whole year

(a) Amount of CENVAT credit attributable to inputs used in or in relation to manufacture of exempted goods on the basis of total quantity of inputs used.

(b) Amount of CENVAT credit on inputs used for provision of exempted services,

$$= \frac{\text{Value of exempted services provided during the financial year}}{\text{Value of dutiable goods manufactured and removed + Value of output and exempted services provided during the financial year}} \times \text{CENVAT credit taken on inputs during the financial year – CENVAT credit attributable to inputs used in or in relation to manufacture of exempted goods}$$

(c) Amount attributable to input services used in or in relation to manufacture of exempted goods and their clearance upto the place of removal or for the provision of exempted services.

$$= \frac{\text{Value of exempted services provided + Value of exempted goods manufactured and removed during the financial year}}{\text{Value of output and exempted goods Manufactured and removed + Value of taxable and exempted services provided during the financial year}} \times \text{CENVAT credit taken on inputs services during the financial year}$$

(d) Pay the difference of provisional duty and final duty determined in point (b) and (c) respectively by 30th June of the succeeding year otherwise interest @ 24% will be charged from due date.

Rule 6(4): If capital goods are exclusively used for exempted goods, cenvat credit on duty paid on such capital goods can not be taken. SSI units are an exception.

For example, capital goods are partly used for exempted services, full credit on them can still be taken.

Rule 6(6): Exception – All clearances made to an 100% EOU, SEZ unit, EHTP, STP U.N.O. etc. and exports made under a bond are eligible for cenvat credit. Although no duty is payable on their clearances as above, input level credit can be taken.

Rule 6(6A): All taxable services provided to a SEZ unit or to a Developer of SEZ without payment of service tax are eligible for CENVAT Credit.

Rule (7): The provisions of sub-rules (1), (2), (3) and (4) shall not be applicable in case the taxable services are provided, without payment of service tax, to a unit in

a Special Economic Zone or to a developer of a Special Economic Zone for their authorised operations or when a service is exported.

Rule (8) For the purpose of this rule, a service provided or agreed to be provided shall not be an exempted service when:-

(a) the service satisfies the conditions specified under rule 6A of the Service Tax Rules, 1994 and the payment for the service is to be received in convertible foreign currency; and

(b) such payment has not been received for a period of six months or such extended period as maybe allowed from time-to-time by the Reserve Bank of India, from the date of provision.”

Rule 7: Manner of distribution of credit by input service distributor

The input service distributor may distribute the CENVAT credit in respect of the service tax paid on the input service to its manufacturing units or units providing output service, subject to the following conditions, namely:—

- (a) the credit distributed against a document referred to in rule 9 does not exceed the amount of service tax paid thereon;
- (b) credit of service tax attributable to service used in a unit exclusively engaged in manufacture of exempted goods or providing of exempted services shall not be distributed;
- (c) credit of service tax attributable to service used wholly in a unit shall be distributed only to that unit; and
- (d) credit of service tax attributable to service used in more than one unit shall be distributed prorata on the basis of the turnover of the concerned unit to the sum total of the turnover of all the units to which the service relates.

Explanation 1.- For the purposes of this rule, unit includes the premises of a provider of output service and the premises of a manufacturer including the factory, whether registered or otherwise.

Explanation 2.- For the purposes of this rule, the total turnover shall be determined in the same manner as determined under rule 5.

Rule 7A: Distribution of credit on inputs by the office or any other premises of output service provider. The provider of output service can take credit on inputs or capital goods on the basis of invoice, challan or bill issued by its other office.

The procedure applicable to first stage or second stage dealer is applicable to the provider of output service.

Rule 8: Storage of input outside the factory of the manufacturer

AC/DC may allow the manufacturer to take cenvat credit on inputs stored outside the factory:

- Such storage is allowed only in exceptional circumstances
- He may allow it by an order

- Nature of goods and shortage of space can be reasons for such order
- The order is subject to certain conditions and limitations that may be imposed by him.

The manufacturer is liable to pay the amount of credit taken on such inputs stored outside if the inputs are not used in the manner specified.

Rule 9: Documents and Accounts [Procedural Aspects]

The cenvat user necessarily has to make sure that he is following the appropriate procedure to avail the cenvat credit. Though no statutory records have been specified by the rules, the user has to maintain proper records on his own and justify his actions in times of doubt/objection raised by the department. Important among them being the duty/tax paying document on the strength of which he has to take the credit. Various types of such documents are namely:

- (a) Invoice obtained from various sources of local purchase. The local suppliers may include manufacturers, importers, dealers or their depots, branches, agents etc.
- (b) Supplementary Invoice: This may be raised by the supplier in addition to the invoice on various counts. The amount paid under this is also eligible for taking cenvat credit but subject to the condition that such issue of supplementary invoice was NOT necessitated by fraud, willful misstatement, suppression of facts etc. on the part of the supplier.
- (c) Bill of Entry in case of direct imports.
- (d) Certificate issued by appraiser of Customs in case of imports by post.
- (e) A challan evidencing the payment of service tax by the person liable to pay service tax.
- (f) An invoice, bill or challan issued by provider of input service.
- (g) An invoice, bill or challan issued by provider of input service distributor.

Rule 9(2): Cenvat credit cannot be taken unless all particulars required in the documents under the provisions are available.

However, the document shall at least contain the following:

- (i) duty/service tax paid
- (ii) description of goods/taxable services
- (iii) assessable value, Registration No. of the person issuing the invoice/bill
- (iv) name and address of supplier/provider of input provider.

AND the AC/DC must be satisfied that the same have been received and accounted for.

On his satisfaction he may allow the credit to be taken.

Returns: Periodical returns on the utilization/transfer of CENVAT credit have to be submitted by various parties as indicated below:

- (i) The manufacturer to file within 10 days in the following month. The SSI within 10 days of the close of the quarter.
- (ii) The FSD/SSD (dealers) to file within 15 days of the close of the quarter.
- (iii) The service provider to file half yearly by the close of the month.
- (iv) The input service distributor shall submit a half yearly return not later than last day of the month following the half year.

The returns are to be submitted to the superintendent of Central Excise. A new format has been issued by the Govt. which has to be adopted for filing the returns.

Under Rule 9(11) the provider of output service or input service distributor may submit a revised return correcting a mistake or omission etc. within 60 days.

Rule 10: Transfer of Credit

The manufacturer or service provider can transfer the credit taken by him in case of transfer of business by way of sale, lease, merger etc. such a transfer must be supported by physical transfer of goods/assets. This must be done by taking into confidence AC/DC and on their satisfaction that everything was done properly.

Rule 11: Transitional provisions

Credit taken under the old rules can be utilized under the New Rules, 2004, such a utilization is subject to the current rules in operation.

If an SSI unit following cenvat credit scheme happens to switchover to nil duty scheme under Notification No. 8/2003, it has to reverse the credit taken on the inventory lying at the time of switchover. If it does not have the credit balance, it has to pay to that extent. If any amount still lies in the credit after the reversal it will automatically lapse forever.

Similarly, when the goods are exempt absolutely, the manufacturer is required to reverse the credit attributable to inputs etc. lying in stock. Any balance remaining will lapse and it cannot be utilized for any purpose whatsoever.

Rule 12: Special dispensation to north eastern states etc.

Certain units in the specified states get preferential treatment. For that purpose various notifications have been issued by the Govt. of India. These units get the exemption benefit of duty paid on value addition. In fact these units pay duty on their final product by availing the input credit. But they will get the refund of the NET amount paid by them on the removal of their final products. This refund is through credit of account current. Yet, it is not treated as exemption for the purpose of cenvat credit utilisation. Consequently, the buyer manufacturer who purchases inputs or capital goods from these units will get cenvat credit normally as if nothing was exempted.

Rule 13: Deemed Credit

This is an exemption to Rule 3, where govt. notifies deemed credit, the amount of credit eligible to be taken is as per the rates notified by the Govt., not on actual basis. At present deemed credit is not in vogue.

Rules 14 and 15 Provide for recovery and penalties for violations under the Rules.

- Recovery: Wrong taking/utilisation or erroneous refund of cenvat credit leads to recovery with interest as per the provisions of Central Excise Act.
- If credit is taken/utilized in contravention, the goods are liable to be confiscated and a penalty not exceeding the amount of duty or ₹ 2,000 whichever is greater is imposed on the manufacturer.
- Similarly, if the credit on input service is taken wrongly or in contravention, penalty upto ₹ 2,000 is payable.
- If fraud, willful misstatement, collusion, suppression of facts or contravention of law is established, the manufacturer is also liable to pay mandatory penalty under Section 11AC of Central Excise Act.
- Similarly for fraud etc. the provider of output service is also liable to penalty under Section 78 of Finance Act, 1994 [Rule 15].

Rule 15A: This new rule provides for general penalty upto ₹ 5,000/- in case of contravention of any of the provisions of the Cenvat Credit Rules for which no specified penal provision exists.

Miscellaneous

Special provisions applicable to units to North east, Kutch dist. of Gujarat Jammu & Kashmir, and Sikkim.

Certain units in above states enjoy exemption from duty on the goods manufactured by them.

There are several notifications such as No. 32/99, 33/99, 39/2001 under which the benefits are passed on to these units subject to conditions to be fulfilled.

The eligible units have to manufacture inputs/capital goods to be used by other units.

The units also have to pay duty on their clearances just like any other unit. But they would get back the amount as credit in their PLA.

Specific Provisions Applicable to these Units

Under Rule 12 of the Cenvat Credit Rules, there is special dispensation to these units.

The excise duties paid by these units on their final clearances will be refunded to them in installments.

Still such a benefit is not treated as exemption.

Consequently, the buyer units are entitled to full credit as shown in the invoice by these units.

Restriction: Second Proviso to Rule 3(4): These units have to necessarily to follow one on one correlation principle for inputs and outputs. That means, when they remove their final products, they should pay duty net after utilizing the Cenvat credit taken on inputs and input services used for the final products.

For example, An eligible unit in North East state purchased some inputs and paid

duty of ₹ 50,000, and took credit of the same. It manufactured some machinery and a duty of ₹ 75,000 is payable on clearance.

In this case the unit should necessarily use the input credit of ₹ 50,000 and pay ₹ 25,000 only and the input credit of ₹50,000 cannot be used for any other product.

Implications: The eligible unit will get the refund of ₹ 25,000.

The buying unit will get full credit of ₹ 75,000 (of course in two financial years on the capital goods).

Special Refund Scheme for these Eligible Units: A new Rule 5A has been inserted in Cenvat Credit Rules, 2004 [Notification No. 24/2007 dt. 25th April, 2007].

This rule 5A provides for the mechanism for refund of unutilized cenvat credit.

This is akin to Rule 5 which gives refund of unutilized credit in respect of exports under a bond or a letter of undertaking.

Refund of Cenvat Credit – Procedure

The Government has prescribed the procedure for claiming refund of the unutilized Cenvat Credit.

1. The manufacturer has to file a declaration with his AC/DC describing the finished goods, duty rate, manufacturing formula with reference to quantity and quality of the raw materials.
 2. A monthly statement by the 7th of the month has to be filed giving details of opening balance, receipts, value, duty, amount of credit taken and quantity of inputs used during the month, final products manufactured, inputs lying in stock, credit utilised and the amount of credit lying in balance.
 3. The AC/DC after verification will refund the unutilized credit within three months from the date of receipt.
- If there is likely to be any delay in granting the refund, the AC can grant 80% of the amount claimed on a provisional basis.

Others:

Reversal of Cenvat Credit: The cenvat credit taken shall be reversed in the following cases:

- Under Rule 11(2), the SSI unit switching over to the exemption scheme has to take stock of inventory lying on the date of switchover, and return the credit attributable to such inventory either by reversing the cenvat credit account or by paying in cash.
- Similarly, when the final products are exempt absolutely, the duty taken on the inventory shall be returned.

Important Note: In both the cases as above, any credit balance still remaining after reversal, shall lapse forever and it cannot be utilized for any purpose whatsoever.

- If obsolete items are totally written off from the books, cenvat credit taken on them shall be reversed.

- However, if the items are partly written off and they are still available in the premises, no reversal of credit is necessary unless they are written off before use.
- If some goods happen to be sold without duty under Central Excise (Removal of Goods at Concessional Rates of Duty for Manufacture of Excisable Goods) Rules, 2001, the cenvat credit attributable to the inputs used for the manufacture of such goods shall be reversed.

No Reversal of credit in the following cases:

- In case of exports/deemed exports
- Intermediate products are supplied without duty where the final products are exported.

No Credit to be taken on the following:

- Shortage of goods received
- Goods lost in transit
- Goods lost in the storage.

Credit however is allowed if the loss as above is normal.

Credit is also allowed if the loss of inputs is during/after the process.

Rule 12A: The large tax payer unit is allowed to transfer inputs or capital goods from the unit to another unit under cover of transfer challan or invoice.

1. The transferee unit should use the inputs for manufacture of final products and clear the goods by payment of duty within a period of 6 months from the date of receipt of inputs.
2. Alternatively the transferee unit can also export final products without payment of duty within six months.

In case of non compliance of the requirements under 1 and 2 above, the recipient unit is liable to pay duty with interest as per provisions under Rule 14 of the Cenvat Credit Rules, 2004.

The recipient unit is entitled to take credit on the inputs and capital goods received.

Rule 12AA. Power to impose certain restrictions: Where Central Government is of opinion that there was misuse of Cenvat Credit, it may provide for some measures including restrictions on utilisation of credit and suspension of registration of FSD/SSD etc. such measures may be taken in public interest.

ELIGIBILITY OF INPUTS AND CAPITAL GOODS – CASE STUDY

1. Low Sulphur Heavy Stock. Naphtha are eligible for credit if they are used for electricity generation where electricity is used for making caustic soda/cement. Solaris Chemtech – 2007 S.C.
2. However, if the electricity is used for staff quarters/schools run by the company, to that extent the credit is not available. Solaris Chemtech – 2007 S.C.

3. Manufacture is not entitled to take credit on input service tax on transport service charges paid to goods transport agency on carriage outward – *Gujarat Ambuja Cements* [TRI, 2007]
4. Inputs need not be used in the factory – *Vikram Cement 2006 (S.C.)*. Explosives used in the blasting of mines to produce limestone in manufacture of cement is eligible as input even if mines situate away from the factory. But mines should be captive mines and they must be an integral part of factory.
5. Durable returnable containers are also eligible as inputs for cenvat credit as they are packing material and a part of it goes to Assessable value – *Chennai Bottling Co.*
6. Building material is not eligible as inputs as they only facilitate manufacture and not used in relation to manufacture – *J.K. Cotton & Spinning Mills*
7. Capital goods extended from factory are eligible [*Manik Garh Cements Ltd.*]. Ropeway extended outside the factory premises are eligible as capital goods as the extension proceeded from the factory.
8. Welding electrodes used in repair and maintenance are inputs eligible for Cenvat credit. [*Manik Garh Cements Ltd. 2007 (Tribunal)*]

Other Relevant Points under Case Law

Held in *Dai Ichi Karkaria Ltd. 1999, S.C.* that no co-relation of inputs and final products is necessary. Cenvat credit taken is indefeasible.

Note: The above decision is subject to the provisions of Rule 3(4) and Rule 11(2).

Cenvat credit is available even on inputs lost or destroyed during process. But if there is loss or shortage during transit, no cenvat credit is available on such lost goods as they were not used in the manufacture.

Education cess and SHE cess are not interchangeable.

No Cenvat credit is allowed on inputs and capital goods lost during storage as they cannot be said to be used in relation to manufacture [*Maruti Udyog Ltd., 2000*]

6.29 Small Scale Industries – Exemptions and Concessions

Vide Notification No. 8 of 2003 Small Scale Industries (SSIs) have an important place in Indian economy. They need special protection as well as favourable treatment. The reasons are many.

- They generate more employment.
- They help in regional development and balanced economic growth.
- More national income and more export earning, and so on.

Concessions under excise have other reasons also. The prices of the goods produced by the SSIs should be competitive and given the level of activity, they deserve some tax concessions. Even the cost benefit analysis is in favour of the SSIs. The cost of collection for SSI is around 5% whereas it is below 1% for large

industries. Hence, government is keen to offer some benefits through various notifications.

What is an SSI?

There is no definition of SSI under excise laws. And the definitions under other laws are not applicable to the scheme under Excise.

Government wants to offer some benefits to small units having small turnover. The units enjoying exemption based on turnover under Excise are called SSIs.

What are the benefits for the SSIs?

The major benefit is exemption, exemption from duty and exemption from registration.

These exemptions are subject to fulfilling the eligibility criteria. The major criteria is turnover of specified goods.

What are the legal provisions providing benefits to SSI units?

The main provisions are under Notification No. 8/2003

SSI Benefit – Two Schemes

<i>Scheme</i>	<i>Status I</i>	<i>Status II</i>
Scheme 1 – Exemption, Without Cenvat Credit Benefit	Upto ₹ 1.5 crore Duty NIL	T.O. above ₹ 1.5 crore Normal Rate of Duty and avail Cenvat Credit
Scheme 2 – Normal – Pay duty & avail Cenvat Credit	Normal Rate of Duty and avail Cenvat Credit	Normal Rate of Duty and avail Cenvat Credit

For eligible units availing exemption under scheme 1 it is automatic and no specific procedure is prescribed. But if the unit wants to switch over from exemption scheme to normal scheme opting to pay duty by availing cenvat credit, it can do any time during the financial year.

Procedure to be followed for switch over/opting to pay duty:

Intimate to the A/C in writing with a copy to the superintendent with details regarding:

- (a) Name and address of the manufacturer
- (b) Location of factory/factories
- (c) Description of the specified goods manufactured
- (d) Date of switch over to the payment scheme
- (e) Aggregate value of clearances.

Notes: Once the unit exercised the option to pay duty, it has to continue till the end of the financial year. If it wants to revert (back) to exemption scheme it can do only in the beginning of the next financial year.

What are the eligibility criteria to get the benefits of the SSI?

1. **Goods**
2. **Turnover**

Goods: must be specified goods which are other than those in the negative list given in the notification No. 8/2003 amended from time to time. Tobacco products, automobiles, explosives, primary iron and steel, ceramics, stainless steel pattas and patties, aluminium circles etc. are in the negative list.

Units manufacturing the above are not eligible for SSI exemption.

In the budget 2008, SSI exemption has been extended to HDPE/PP tapes consumed captively in the manufacture of sacks/bags. [effective from 1st April, 2008]

The honorable Supreme Court in *CCE v. Khanna Industries* 2007 S.C. held that SSI exemption is goods specific.

But the goods, subject to some exceptions, shall not bear the brand name of others.

Exceptions: In the following cases, the goods bearing the brand name/trade name of others will be eligible for SSI exemption.

1. Components or parts of machinery, equipment or appliances cleared for use as original equipment in the manufacture of the said machinery, equipment appliance.
2. The exemption is available for the goods bearing a brand name of:
 - The State Khadi and Village Industry Board
 - Khadi and Village Industries Commission
 - The National Small Industries Corporation
 - A State Small Industries Development Corporation; or
 - A State Small Industries Corporation
3. Where the specified (eligible) goods are manufactured in a factory located in a rural area, they are eligible even if they are bearing the brand name of others.
4. Account books, registers, writing pads and file folders under chapter 48 of CETA.
5. Items in the nature of packing material.
6. Printed laminated rolls.

Conclusion: The goods to be eligible must be specified goods and further they should not bear the brand name of others – subject to certain exceptions.

Turnover in previous financial year is the basis for eligibility in the current financial year.

When the turnover is not above ₹4 crore in the previous financial year, the unit will be eligible to enjoy exemption from duty upto ₹1.5 crore turnover in the current financial year.

For example, A manufacturer is manufacturing marble slabs and tiles under Chapter 25 of the Tariff Act.

His turnover in the previous financial year was ₹ 3.8 crore.

Is he eligible for exemption in the current financial year?

Yes. Reasons: 1 Marble goods are eligible for SSI exemption. 2. The turnover is less than ₹ 4 crore.

Turnover – Related Issues: Turnover is a critical factor in deciding the eligibility.

What is turnover under the scheme?

It is the value (assessable value) of clearances in a given financial year. The value is as determined under Section 4, 4A or 3(2) of Central Excise Act as the case may be.

Turnover means turnover of goods manufactured. Obviously, inputs, partially processed goods or capital goods removed as such are not to be considered as turnover.

- Goods means excisable goods – non excisable goods can not be considered for turnover.
- Goods means own branded goods/unbranded goods – others branded goods are not considered.
- Goods means finished goods, not intermediate goods.
- Goods means own goods, not those goods manufactured as a job worker availing exemption.
- Goods means dutiable goods – not nil rated goods.

Turnover means turnover of local clearances, not export turnover.

But

- Export to Nepal and Bhutan is a local clearance
- Outright sale of goods to an exporter is a local clearance.

What is export turnover?

1. Direct exports 2. exports through merchant exporter 3. Deemed exports, eg. sale to E.O.U. EHTP, STP SEZ units, UNO Agencies or international agencies without duty.

Illustration: Find out turnover from the following clearances made in the previous financial year.

	₹
Local sale	2.6 crore
Export to Nepal under foreign currency	1.2 crore
Sale to an E.O.U.	1.75 lac
Intermediate products manufactured as job worker and availed exemption Notification No. 214/86	23,000

Sale of inputs after partial process not amounting to manufacture	34,000
Exports to China	44 lac
Sale to UNO Agencies under exemption notification	1.7 lac
Clearance of nil rated goods	2.8 crore
Goods of others brand cleared (50% of them were manufactured in a rural area)	0.2 crore

₹ in crore

Local clearances as per SSI notification:

1. Local sale	2.6
2. Export to Nepal	1.2
3. 50% of branded goods manufactured in rural area	<u>0.1</u>
	<u>3.9</u>

Notes: Export to Nepal in any currency is a local clearance.

When goods of other brand are manufactured in rural areas they are eligible for SSI exemption and hence includible in turnover.

Important Note: Turnover of exemption goods is included for calculating ₹ 400 lac but same is not includible for calculating ₹ 150 lac.

Clubbing of Turnover: The following turnovers are clubbed together to calculate the turnover achieved

- by a manufacturer from all of his factories wherever they are located
- by different manufacturers in the same factory, during different shifts or same shifts
- by different manufacturers in the same factory, during different parts of a year.

Question: If a factory has been operated during any financial year by different owners/operators/persons, how will the eligibility for excise duty concessions available to SSI units be determined?

Ans.: The turnover of all the manufacturers will be added to calculate ₹ 400 lakh/150 lakh.

Question: Vishnu, your old class mate, operates a manufacturing unit having two factories with turnover of ₹180 lakh and ₹ 145 lakh respectively in the previous year 2011-2012. He seeks your advice whether his unit is eligible for exemption as is available to SSI units.

Ans.: The combined turnover of both the factories is ₹ 325 lakhs which is less than ₹ 400 lakhs. Hence both the units of Vishnu are eligible for SSI exemption if the goods manufactured are specified goods.

Ans.: The turnover of both the firms is includible irrespective of their independence.

No Clubbing of Turnover: In the following cases, turnover is not to be clubbed.

- If two or more factories (separate premises) have common partners, common directors.
- Clearances of manufactured goods of raw material supplier can not be clubbed with the Clearances of independent manufacturer/job worker.
- Turnover of subsidiary Co. with that of holding Co. Catalco Chemicals, 2006 (Tri)
- Units belonging to government e.g. The State Khadi and Village Industry Board Khadi and Village Industries Commission; The National Small Industries Corporation.

Conclusion: Turnover of two or more units of same ownership is subject to clubbing:

- Turnover of different independent owners is includible only if the activity is in the same factory.
- Turnover of different owners of different factories can not be clubbed even if there is some relation or commonness.
- Turnover of two independent units can not be clubbed.
- Turnover of two units can be clubbed if they are dummy units in different names but owned and controlled by same person/persons.

Brand Name under SSI Scheme: Subject to exceptions, goods bearing the brand name or trade of others are NOT eligible for exemption under SSI scheme. The basic idea is to protect only unbranded/own branded goods. Units enjoying the support of others brand or trade name are debarred from enjoying the privilege of SSI status.

What is a brand name?

Brand name or trade name means

- A name, mark such as a symbol, monogram, label, signature or invented word
- Used in relation to such specified goods for indicating connection in the course of trade
- Between the goods and some person using the brand name with or without indicating the name of that person
- Such brand name or trade name need not be registered under the Trade Marks Act, 1999.

What is the object of disqualifying small units using other brand name?

In Bhalla Enterprises, 2005 (S.C.) the Supreme Court held that the object of notification is to grant benefit to those industries which do not have the advantage of a brand name (of others). It is neither to protect the consumer nor the owner of the trade mark.

Other Concessions to SSI Units: Besides the duty exemption, the SSI units enjoy many more concessions in terms of procedures.

The following table illustrates the same:

<i>Subject Matter</i>	<i>Relaxation</i>
Return	Quarterly Return in Form ER-3 by the 10 th of the following quarter.
Payment of duty	Quarterly by 5 th of the following quarter or by 6 th in case of e-payment
Registration	No registration upto the turnover of ₹ 150 lakhs. Only a declaration on reaching the turnover of ₹90 lakhs
Simplified export procedure	ARE form need not be filed for units with turnover below ₹ 150 lakh
Official visits	Only with prior approval of A/C the SSI unit can be visited by officers of excise
Audit	Only once in 2 to 5 years

Important Notes

1. small scale industry has nowhere been defined in excise laws. The benefits availed by units based on value of clearances are a clue to it. Those units manufacturing eligible goods specified in the notifications, and also qualifying the test of annual turnover are considered as small scale industries.
2. to get the beneficial treatment under the notification 8/2003, the qualifying tests are: manufacture of eligible goods and their previous financial year's turnover being not more than ₹ 4 crore.
3. once the unit qualifies the above twin tests, the unit will enjoy the benefits of the notifications in the current year.
4. these benefits are available upto one crore, fifty lakh turnover in the current year.
5. switch over from exemption scheme to normal duty scheme can be made any time during a financial year but vice versa not possible.
6. once opted for normal duty scheme, the unit can take cenvat credit on inventory lying with it on the date of switch over.
7. similarly, when reverted to exemption scheme, effective from 1st of April, it has to reverse the cenvat credit attributable to the inventory available with it on 1st April.
8. simultaneous availment of cenvat credit and exemption is not allowed. It means single scheme for all products has to be adopted uniformly.

In the budget 2007, the exemption limit has been raised to 1.5 crore rupees.

The following table shows the turnover which is excluded for the purpose of calculating ₹ 4 crore and/1.5 crore in the previous year and current year respectively.

Exclusion – A Comparison

No.	For 1.50 lakhs in the Current Financial Year	For 400 lakhs in the Previous Fin. Year
1.	Export turnover direct and through merchant exporter. [Except export to Nepal and Bhutan]	Same [excluded]
2.	Deemed exports – Sale to EOUs, SEZ, EHTP/STP	Same [excluded]
3.	Goods of others brand	Same [excluded]
4.	Manufacture of intermediate product captively consumed unless the final product is generally exempt.	Same [excluded]
5.	Job work amount to manufacture not availing exemption notification No. 214/86	This turnover is included.
6.	Nil rated/exempted goods	Only nil rated goods excluded
7.	Inputs removed as such without processing	Same [excluded]

Cenvat Credit Implications and Applicable Provisions

- The SSI unit after crossing the turnover limit of ₹ 1.5 crore, can start availing and utilizing cenvat credit.
- Before reaching the turnover of 1.5 crore it can avail cenvat credit on capital goods as per Rule 6(4) of Cenvat Credit Rules, but cannot utilize the same under the notification. It means it can start utilizing the credit on capital goods only when its turnover goes beyond ₹ 1.5 crore.
- When the eligible SSI unit wants to go back to exemption scheme, it can do only in the beginning of the financial year. As per rule 11(2) of Cenvat Credit Rules, at the time of switch over, it has to pay the amount of duty attributable to the inventory lying as stock by debiting the cenvat credit account or otherwise any balance remaining after writing off, will lapse and it cannot be utilized for any purpose whatsoever.

6.30 Conclusion

As would emerge from the foregoing, the Excise Law contains very elaborate schemes to question, at several stages within the Department, any decision made or order passed by any officer of the Department. As there are always two sides to every dispute, matching facilities are given at each stage, for either side (that is, the assessee and the Department). While the law is comprehensive, and the procedures quite elaborate, grievances are however often heard that the machinery as a whole moves at exasperatingly slow speed. The Department, cognizant of the existence of some merit in such a view, is constantly on the look out to curtail delays.

The reasons for the situation are not far to seek. Any scheme which gives ample opportunities for either party to the same dispute to contest each matter at each

stage, should necessarily entail considerable consumption of time before the final decision emerges. The volume of work generated in the area of appeals is of gigantic dimensions, and this also is a factor contributing to the time taken by the appellate bodies. While the Department will continue its endeavour to increase the pace, perhaps industry and trade can also contribute to a substantial extent in this regard by reducing the workload on the appellate bodies. This could be by resisting the temptation to which most assesseees are seen easily to succumb. The temptation is to take up before the appellate authorities cases which even the appellants themselves know, do not have a semblance of a chance to succeed. Appeals should not be considered as a kind of ritual to be gone through, after every decision is made or order passed by any departmental officer.

ANNEXURE 1

**PROVISIONS OF THE CUSTOMS ACT AND THE CENTRAL
EXCISE ACT PERTAINING TO APPEALS**

— A Bird's Eye View

<i>Sl. No.</i>	<i>Subject</i>	<i>Customs Act, 1962</i>	<i>Central Excise Act, 1944</i>
(1)	(2)	(3)	(4)
1.	Appeals to Commissioner (Appeals)	Sec. 128	Sec. 35
2.	Procedure in Appeal	Sec. 128A	Sec. 35 A
3.	Appeals to the Appellate Tribunal	Sec. 129A	Sec. 35 B
4.	Orders of Appellate Tribunal	Sec. 129B	Sec. 35 C
5.	Procedure of Appellate Tribunal	Sec. 129C	Sec. 35 D
6.	Powers of Board or Commissioner Central Excise to pass certain orders	Sec. 129D	Sec. 35 E
7.	Powers of revision of Board or Commissioner of Central Excise in certain cases	Sec. 129DA	Sec. 35 EA
8.	Revision by Central Government	Sec. 129 DD	Sec. 35 EE
9.	Deposit, pending appeal of duty demanded or penalty levied	Sec. 129E	Sec. 35 F
10.	Statement of case to High Court	Sec. 130	Sec. 35 G
11.	Application to High Court	Sec. 130A	Sec. 35 H
12.	Power of High Court or Supreme Court to require statement to be amended	Sec. 130B	Sec. 35 I
13.	Case before High Court to be heard by not less than 2 Judges	Sec. 130C	Sec. 35 J
14.	Decision of High Court or Supreme Court on the case stated	Sec. 130D	Sec. 35 K

15.	Appeal to the Supreme Court	Sec. 130E	Sec. 35 L
16.	Hearing before Supreme Court	Sec. 130F	Sec. 35 M
17.	Sums due to be paid notwithstanding reference etc.	Sec. 131	Sec. 35 N
18.	Exclusion of time taken for copy	Sec. 131 A	Sec. 35 O
19.	Transfer of certain pending proceedings and transitional provisions	Sec. 131B	Sec. 35 P
20.	Appearance by Authorised Representatives	Sec. 146A	Sec. 35 Q
21.	Definitions	Sec. 131C	Sec. 36

ANNEXURE 2

Note: Students are required to be familiar with the Performa of appeals, a reference to which can be had from the Central Excise Manual. The following 'Forms of Appeals' are relevant for this purpose:

<i>S.No.</i>	<i>Subject/ Form No.</i>	<i>Central Excise Act, 1944 (Sections)</i>	<i>Central Excise (Appeals) Rules, 2001</i>
1	Form of Appeal to the Commissioner (Appeals) E.A.-1	35	3(1)
2	Form of Application to the Commissioner (Appeals) E.A.-2	35E(4)	4
3	Form of Appeal to Appellate Tribunal E.A.3	35B	6(1)
4	Form of Memorandum of Cross-objections to the Appellate Tribunal E.A.-4	35B	6(2)
5	Form of Application to Appellate Tribunal E.A.-5	35E(1)	7
6	Form of Reference Application E.A.-6	35H(1)	8(1)
7	Form of Memorandum of Cross-objections to the Appellate Tribunal in the matter of Reference to the High court E.A.-7	35H(3)	8(2)
8	Form of Revision Application to the Central Government E.A.-8	35EE(3)	9(1)

LESSON ROUND UP

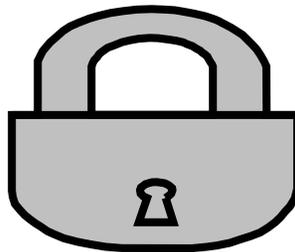


This Chapter includes:

- Basis of Levy of Excise Duty
- Basis of Chargeability of Excise Duty
- Concept of “Goods”
- Concept of “Excisable Goods”
- Production, Manufacture and Process distinguished
- Concept of “Manufacturer”
- Classification of Goods
- Valuation of Goods Under Central Excise Law
 - Methods of Valuation
 - Valuation Based on MRP
 - Scope and objects
 - Valuation under Section 4
 - Transaction Value
- Procedure for fixation of value under Section 4
- The Central Excise Valuation (Determination of Price of Excisable Goods) Rules, 2000
- The Central Excise (Determination of Retail Sale Price of Excisable Goods) Rules, 2008
- Payment of Excise Duties
- Clearance and Removal Procedures
 - Self Assessment Method
 - Removal of goods on invoice
 - Compounded Levy Scheme
- Remission of Duty (Rule 21)
- Filing of return and E-Filing of return
- Large Tax Payer Units
- Excise Duty — Exemptions
- Recovery of sums due to Government (Section 11)
- Recovery of duties not levied or not paid or short levied or short paid or erroneously refunded (Section 11A)
- Interest on delayed payment of duty (Section 11AA)
- Claim for refund of duty and interest, if any paid on such duty (Section 11B)
- Doctrine of Unjust Enrichment
- Payment of Interest on delayed refund (Section 11BB)

- Power not to recover duty of excise not levied or short levied as a general practice (Section 11C)
- Excise Audit - 2000
- Deposit of Central Excise Duty During Strikes in Nominated Banks
- Appellate Procedures and Search, Seizure and Investigation
 - The Appellate Scheme
 - The Customs, Excise, Service Tax Appellate Tribunal (CESTAT)
 - Appeals before Commissioner (Appeals) (Section 35)
 - Further remedies after decision by CESTAT
 - Powers of Committee of Chief Commissioners of Central Excise or Commissioner of Central Excise to pass certain orders on its own (Section 35E)
- Deposit Pending appeal of duty demanded or penalty levied (Section 35F)
- Interest on delayed refund of amount deposited under the proviso to Section 35F (Section 35FF)
- Revisionary Role of the Central Government
- Settlement Commission
- Powers and Duties of Officers
- Power of Adjudication
- Procedure to be followed in cases where duty is paid under protest
- Special Audit in certain cases (Section 14A)
- Special Audit in cases where credit of duty availed or utilized is not within normal limits etc. (Section 14AA)
- CENVAT Credit Rules 2004
- Small Scale Industries
- Conclusion
- Annexures

SELF-TEST QUESTIONS



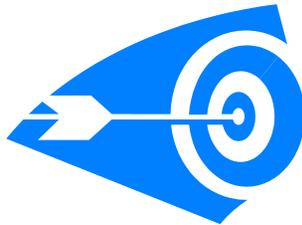
(These are meant for recapitulation only. Answers to these questions need not to be submitted for evaluation).

1. What Appellate Scheme has been provided under the Central Excise?
2. What is the procedure for filing Appeal before Commissioner (Appeals)?
3. Discuss the circumstances under which Department may order for re-opening of its original orders/decisions and the procedure it has to follow in this regard.

4. Under what circumstances the original orders/decisions may be re-opened by the department?
 5. What is the procedure required to be followed for re-opening of original orders/decisions?
 6. Under what circumstances a stay may be granted on the operation of original orders?
 7. What is the objective of Excise officers being given powers of access, search and seizure?
 8. What are the powers of authorised officers with regard to Access, Search, Seizure where Excisable goods are involved.
 9. What are the provisions with regard to confiscation and penalty under Central Excise Rules, 2002?
 10. What is the difference between seizure and the confiscation?
 11. State the provisions relating to storage charges in respect of confiscated goods.
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STUDY VII
CUSTOM LAWS

LEARNING OBJECTIVES



The objective of this chapter is to discuss the following topics/concepts:

- Introduction
- Taxable Event
- Types of duties under Custom
- Tariff classification
- Valuation of Goods For Levy of Customs Duty
- Customs Valuation (Determination of Price of Imported Goods) Rules, 2007
- Custom Valuation (Determination of Value of Export Goods) Rules, 2007
- Determination of Rate of Duty And Tariff Valuation
- Remission, Exemption and Demands in Customs
 - Duty on Pilfered goods
 - Re-Importation of Goods
 - Goods derelict, wreck, etc.
 - Abatement of duty
 - Remission of duty on lost, destroyed and abandoned goods
 - Exemption from duty
 - Policy guidelines for ad hoc exemption under Section 25(2)
 - Refund of Duties
- Recovery of Duties
- Recovery of duties not levied or short levied or erroneously refunded under Section 28
- Power not to recover duties
- Interest on delayed payment of duty under Section 28AA
- Recovery of duties in certain cases under Section 28AAA
- Assessment of duty (Section 17)
- Provisional Assessment of duty (Section 18)
- Advance Ruling
- Clearance of Imported or Exported Goods Including Baggage
- Assessable Value and Levy of Duty—Method of Assessment

- Clearance of Export Cargo
- Customs procedure – Documentation for Export
- Shipment (Export) under claim for drawback
- Procedure for Exports through inland Container Depots
- Procedure for Exports of Contenerised Cargo from Inland Container
- Baggages
- Goods Imported or Exported by Post
- Stores
- Provisions Relating to Coastal Goods and Vessels Carrying Coastal Goods
- Duty Drawback
- Transportation of Goods
- Warehousing
- Adjudication and appellate provisions:
- Powers of Committee of Chief Commissioners of Customs or Commissioners of Customs to pass certain orders (Section 129D)
- Appeal to Supreme Court (Section 130E)
- Deposit, pending appeal, of duty and interest demanded or penalty levied
- Interest on delay payment of Refund (Section 129EE)
- Customs (Appeals) Rules, 1982
- Settlement Commission
- Customs and Central Excise Settlement Commission Procedure, 2007
- Search, Seizure, Arrest, Confiscation Etc.
- Confiscation of Goods
- Adjudication of confiscation and penalties
- Option to pay fine in lieu of confiscation
- Award of confiscation or penalty by Customs Officers not to interfere with other punishments
- Offences and Prosecution Provisions
- Miscellaneous Provisions

7.1 INTRODUCTION

Customs Act, 1962 just like any other tax law is primarily for the levy and collection of duties but at the same time it has the other and equally important purposes such as: (i) regulation of imports and exports; (ii) protection of domestic industry; (iii) prevention of smuggling; (iv) conservation and augmentation of foreign exchange and so on. Exports especially have a little significance from the revenue point of view. Even imports under the regime of WTO commitments face reduction in the rates of duty.

As there are three stages in any tax structure, viz., levy, assessment and collection, the first one is in the hands of the legislature. Legislature, by fulfilling the requirements of the Article 265 imposes the tax liability attached to its taxable event.

Under customs, the taxable events are – import of goods into or export of goods out of India. Section 12 is a charging Section which lays down the conditions of levy of custom duty.

Conditions of Levy: As per Section 12, customs duty is imposed on goods imported into or exported out of India as per the rates specified under the Customs Tariff Act, 1975. The provisions are equally applicable to goods belonging to the Government.

On analysis of Section 12, we derive the following points:

- (i) Customs duty is imposed on goods when such goods are imported into or exported out of India;*
- (ii) The levy is subject to other provisions under this Act or any other law;*
- (iii) The rates of duty are as specified under the Custom Tariff Act, 1975;*
- (iv) Even goods belonging to Government are subject to levy, though they may be exempted by some notifications under Section 25.*

7.2 TAXABLE EVENT

The basic condition for levy of customs duty is import/export of goods i.e. goods become liable to duty when there is import into or export from India.

- Import means bringing into India from a place outside India [Section 2(23)].
- Export means taking out of India to a place outside India [Section 2(18)].
- "India" includes the territorial waters of India [Section 2(27)]. The limit of the territorial waters is the line every point of which is at a distance of twelve nautical miles from the nearest point of the appropriate baseline.

Though the taxable event is import/export but yet it is difficult to determine the exact time of levy.

Case Laws:



This issue has been further complicated by conflicting decisions by various High Courts.

1. In *Chetan Kumar & Co. v. C C* 1988(33) ELT (Madras):

The Madras High Court held that chargeability arises when the imported goods get mixed up with the land mass of India and the chargeability takes place at the time of unloading the goods. Earlier, in *Apar Private Ltd. v. U.O.I.* 1985 (22) ELT 644 Bombay High Court held "the taxable event occurs no sooner the goods enter the territorial waters of India and doesn't postpone till they are actually off-loaded on the land mass or till the goods are valued under Section 14 or till the date for determining the rate at which customs duty should be levied under Section 15 arrives...."

2. *U.O.I. v. Apar Private Ltd.* 1999 (112) S.C. ELT 3:

There were thus, many conflicting judgements and until the matter had been decided by the Supreme Court in an appeal preferred by the Union of India in *Apar Private Limited* (supra). The Honourable Supreme Court overruled the full bench decision of the Bombay High Court and held that the rate of duty applicable to any imported goods is the date determined in accordance with Section 15(1) of Customs

Act as (a) in the case of goods cleared for home consumption, the date of presentation of Bill of Entry under Section 46 or the date of grant of entry inwards to the vessel, whichever is later and (b) in case of goods from bonded warehouse the date of actual removal from the warehouse.

Date when vessel enters territorial waters is irrelevant

The goods in the instant case had been imported and were deposited in the warehouse pending the final clearance. They were under exemption from duty both at the time of import and deposit in the warehouse. Subsequently, at the time of clearance from warehouse for home consumption, the exemption was withdrawn by the Govt. and consequently, the goods became dutiable. The question arose whether duty liability is determinable at the time of import or at the time of actual removal of warehoused goods. The Bombay High Court had earlier given its verdict in favour of the assessee saying that the taxable event is complete when the goods cross the territorial waters of India. But the S.C. overruled the decision saying that the taxable event is complete when the goods are finally cleared from the warehouse. Hence, the rate prevailing at the time of removal of goods from the warehouse is applicable.

3. *Garden Silk Mills Ltd. v. U.O.I.* 1999 S.C. ELT 358

Held that import of goods in India commences when the goods enter into territorial waters but continues and is completed when the goods become part of the mass of goods within the country. The taxable event is reached at the time when the goods reach customs barrier and Bill of Entry for home consumption is filed.

In case of warehoused goods, the goods continue to be in customs bond. Hence, import takes place only when goods are cleared from the warehouse.

4. *Kiran Spinning Mills v. C.C.* 1999 (113) 753 S.C.

The same three members bench of the Supreme Court which decided the Garden Silk Mills case held that import is completed only when goods cross the customs barrier. The taxable event is the day of crossing the customs barrier and not on the date when goods landed in India or had entered territorial waters of India.

In case of goods which are in the warehouse, the customs barrier would be crossed when they are sought to be taken out of the customs and brought to the mass of goods in the country.

The above decisions of the apex court set at rest the controversy of the taxable event for imports. Taxable event as may be recalled, is the event or situation which gives rise to tax liability. The controversy was whether the taxable event of imports is complete when goods enter the territorial waters of India or when they cross the customs barriers. The S.C. has supported the latter.

The goods imported may be cleared immediately for home consumption (i.e. for use within the country) or for deposit of goods in the bonded warehouses without duty. In the case of clearance of goods for home consumption, the taxable event is reached on goods reaching the customs barrier and the same is completed when they become part of the mass of goods within the country.

In this case, when the imported goods are deposited in a warehouse, the taxable event is postponed till they are cleared from such warehouse. Accordingly, the rate of

duty relevant on the date of clearance is as applicable under Section 15, it may be noted that the definition of India under Section 2(27) interpreted by the Madras High Court in *M Jamal & Co.* has been approved by the Supreme Court.

Having gone into the judicial view of the meaning of the term India in Section 12, it is appropriate to go back at this stage, to the discussion.

The Customs Tariff Act is an important fiscal enactment designed to raise revenue and to promote the economic development of the country as well, by varying the rates of duty. The power to vary the rates of duty from time to time is implicit in the power to impose duties. In this connection, it is to be noted that in terms of Section 12(2) of the Customs Act, 1962, the goods belonging to Government are also liable to pay Customs duty.

Customs duty on import and export is being levied and collected on the basis of the Customs Tariff Schedule, which is based on the Harmonized Commodity Description and Coding System. When the Harmonized system prescribes the rates of duties represented as “%”, it means that the duty has to be levied at the rates specified in the Schedule “on the value of the goods” (*Ad valorem*). This is, generally, the case. If however, in certain instances, the rate can also be prescribed as, “so many rupees per unit of measure”. Such a rate is called a “specified rate”. At times, both methods are resorted to and a combined rate format is used, such as, “so many % *ad valorem* + so much per kg. or metre”.

7.3 TYPES OF DUTIES UNDER CUSTOMS

There are various types of Customs import duties:

1. Basic Duty: It is levied under Section 12 of Customs Act, 1962, and specified under Section 2 of the Customs Tariff Act, 1975. There are different rates for different goods. The general basic rate may varies from 5% to 40%. This basic duty may be exempted by a notification under Section 25. The basic duty may have two rates under the First Schedule to Customs Tariff Act, 1975; viz. standard rates and preferential rates.

2. Standard and Preferential Rates: Duty at the “Standard rate” is charged where there is no provision for preferential treatment. To be eligible, for the preferential treatment the goods should be the one imported from any preferential area covered under the Government of India Agreements for charging preferential rate of duty. The Central Government has the power to increase or reduce or discontinue the preferential rate in respect of any article specified in the First Schedule provided it considers it to be necessary in the public interest. Preferential rate is applied only where the owner of the article (importer) claims at the time of importation, with supporting evidence, that the goods are chargeable with the preferential rate of duty.

3. Additional Duty/Countervailing Duty: This is levied under Section 3 of the Customs Tariff Act, 1975. The amount is equivalent to the amount of excise duty payable on such goods manufactured in India. In *S.K. Patnaik v. State of Orissa*, 2000 S.C. it was held that countervailing duty is imposed when excisable articles are imported in order to counter balance the excise duty, which is leviable on similar goods if manufactured within the State:

— Countervailing Duty is payable at effective rates.

- When excise duty is exempt/nil rate is applicable on goods imported, no Countervailing Duty is levied.
- Countervailing Duty is leviable even if similar goods are not produced in India.
- Exemption of basic customs duty doesn't automatically mean exemption of Countervailing Duty.
- Countervailing Duty is payable in case of goods leviable under State excise also.
- When the imported goods are valued under Section 4A [valuation based on retail price], the amount of Countervailing Duty is calculated accordingly if the goods are sold in retail in India.

4. Education Cess: An education cess has been imposed on imported goods w.e.f. 9.7.2004. The cess will be 2% of the aggregate duty of Customs. However, education cess will not be payable on safeguard duty under sections 8B and 8C, countervailing duty under section 9, anti Dumping duty under sections 9A of the Customs Tariff Act. Further Additional Duty payable under section 3(5) will also not be considered while calculating education cess. Secondary and Higher Education Cess is payable at 1%.

5. Additional Duty under section 3(5): It is levied to offset the effect of sales tax, VAT, local tax or other charges leviable on articles on its sale, purchase or transaction in India. It is leviable on imported goods even if article was not sold in India.

Special CVD [Section 3(5)] (also known as SAD)

- This is imposed on imported goods in addition to other duties if any.
- This is in lieu of sales tax.
- It is levied on all goods subject to exemption at a fixed rate of 4%.

Exemptions:

- All goods exempt under VAT are also exempt from Spl. CVD.
- When BCD and CVD are exempt, this is also exempt.
- Baggage is exempt.
- EOUs, EHTPs & STPs are exempt for their DTA clearances.

6. Protective Duty - Section 6 of the Customs Tariff Act, 1975

- The objective is to protect the indigenous industry from the imports. Tariff Commission has been established under the Tariff Commission Act. Upon a reference, the Tariff commission makes recommendations to Central Government.
- If the Central Government is satisfied with the recommendation, it issues a notification.

- Once the notification is issued, it should be placed as a Bill in the Parliament when in session. Bill should be passed within 6 months of its introduction. Otherwise, the notification ceases to have effect. But, action already taken remains valid.
- The rate of duty can be altered, by releasing a fresh notification.
- The protective duty is not acceptable under W.T.O.

7. Safeguard Duty - Section 8B of Customs Tariff Act

- The Central Government may impose safeguard duty on specified imported goods, if it is satisfied that the goods are being imported in large quantities and they are causing serious injury to domestic industry”
- This duty can be imposed only for a limited period, by way of a notification, after an enquiry.
- It can be imposed provisionally for a maximum period of 200 days.

8. Anti-Subsidy Duty (Duty on Bounty Fed Articles) - Section 9 of the Customs Tariff Act

- If the exporting country pays any subsidy (directly or indirectly) to its exporters for exporting goods to India, the Central Government may impose this duty, by a notification.
- The amount of duty can be maximum upto the amount of subsidy.
- If the amount of subsidy cannot be ascertained, it may be collected on provisional basis.
- Upon final determination, adjustments are made to the duty collected provisionally.

9. Anti-dumping Duty (ADD) - Section 9A of the Customs Tariff Act

- Dumping means exporting goods to India, at prices lower than the ones in the domestic market of the exporting country, subject to certain adjustments.
- To prevent dumping, the Central Government may levy ADD upto margin of dumping. [MOD].
- MOD is the difference between the normal value and the price charged for exports to India.
- Normal value means comparable price in the ordinary course of trade, in the exporting country, after making adjustments to the extent of conditions of sale, taxation, etc.

10. National Calamity Contingent Duty (NCCD): It is levied on pan masala, chewing tobacco and cigarettes, motor cars, crude oil etc.

Steps in determining the amount of duty payable :

Duties of Customs become payable when there is import into India. Accordingly, customs duty would be levied on such goods and the amount of duty has to be

determined. There are several types of duties leviable on import and there are prescribed methods of computation of duties. It is useful to consider the following steps in determining the amount of duty payable.

- (1) Obtain the Tariff Classification of goods.
- (2) Compute the: (i) Basic Customs Duty; (ii) Surcharge; if any (iii) Additional Duty of Customs (equal to excise duty); and (iv) Special Additional Duty.
- (3) Determine if there are any additional levies under different statutes.
- (4) Whether there are concessions and exemptions available on the item.

7.4 TARIFF CLASSIFICATION

Since there are thousands of different goods, which are imported into India, it is not possible to prescribe rates of duty for each type of merchandise. Therefore, all goods are classified into categories (called “headings” and “sub-headings”) for the purpose of levy of duty. For each sub-heading, a specific rate of duty has been prescribed. The process of assigning the goods to a “headings” or a “sub-heading” is known as “Classification of Goods” i.e. determination of heading or sub-heading under which a particular item is covered. The classification is as per the Schedules to the Customs Tariff Act, 1975, commonly referred to as the tariff and is based on the Harmonized System of Nomenclature (HSN) which has been established by the World Customs Organization.

The import invoice would indicate all items of purchase. If you wish to compute the total duty payable on each of the items, you have to first identify the various types of duties leviable on each of the items. For this purpose, you are required to determine the classification of each of the items of import as given in the import invoice based on your understanding of the item description. The rules to be followed while determining the classification have been given in the General Rules of Interpretation of the First Schedule to the Customs Tariff Act, 1975.

7.4.1 COMPUTATION OF THE (I) BASIC CUSTOMS DUTY (II) SURCHARGE (III) ADDITIONAL DUTY OF CUSTOMS (IV) SPECIAL ADDITIONAL DUTY UNDER THE CUSTOMS TARIFF ACT, 1975 AND OTHER LAWS

Above are the various types of duties which are leviable. As a first step, the following three types of customs duties have to be computed:

- (i) *Duty* which is specified against each Heading or Sub-heading in the First Schedule to the Customs Tariff Act, 1975. This is usually referred to as Basic Customs Duty. There are different rates of duties for different commodities. You may find these rates in column no. 4 (labelled as “standard rates”) of the tariff. There is also column No. 5 specifying the “preferential rates”. These are different rates of duties for goods imported from certain countries in terms of bilateral or other agreements with such countries -which are called preferential rates of duties. The duty may be a percentage of the value of the goods (in such cases it is called ad valorem duty) or at a specific rate, which is based on unit of measurement which is specified in the tariff entry. The rate of duty in percentage (in the case of ad valorem duties) has to be applied on the Cost Insurance and Freight [C.I.F.]

- (ii) **Additional duty** of customs equal to the excise duty leviable on like goods produced or manufactured in India. This is levied under Section 3 of Customs Tariff Act, 1975. This is usually referred to as “countervailing duty” (CVD). However, the correct description of this duty is Additional Duty of Customs. In order to determine the applicable rate, you have to obtain the correct classification of the goods under Central Excise Tariff Act, 1985. The duties under the Central Excise Tariff are levied on ad valorem basis. However, specific rates have been prescribed for some items. Importantly, the value for the purpose of computing additional duties of Customs is the total of the assessable value (generally the transaction value - roughly equal to the C.I.F. value) and the basic customs duty.

If you are a manufacturer, importing goods to be used as inputs for manufacture of other goods, you would be generally eligible for obtaining credit (called CENVAT credit) equal to the additional duty of customs paid on the imported goods. This duty amount is eligible for credit. This credit can be used for paying central excise duties on your manufacture.

- (iii) **Education Cess:** An education cess has been imposed on imported goods w.e.f. 9.7.2004. The cess will be 2% of the aggregate duty of Customs. However, education cess will not be payable on safeguard duty under section 8B and 8C, countervailing duty under section 9, anti Dumping duty under section 9A of the Customs Tariff Act. Further Additional Duty payable under section 3(5) will also not be considered while calculating education cess. SHE cess is payable at 1%.
- (iv) **Additional/Special Countervailing Duty under section 3(5):** This duty is leviable on any imported articles in order to counter balance the sales tax, value added tax, local tax or any other charges for the time being leviable on a like article on its sale, purchase or transportation in India. It is leviable at a rate not exceeding four per cent of the value of the imported article. It is applicable to both agricultural as well as industrial products. This additional duty is not includible in the assessable value for the levy of Education Cess on imported goods. Manufacturers shall take credit of this additional duty for payment of excise duty on their furnished products.

The expression “sales tax, value added tax, local tax or any other charges for the time being leviable on a like article on its sale, purchase or transportation in India” means the sales tax, value added tax, local tax or other charges for the time being in force, which would be leviable on a like article if sold, purchased or transported in India or, if a like article is not so sold, purchased or transported, which would be leviable on the class or description of articles to which the imported article belongs and where such taxes, or, as the case may be, such charges are leviable at different rates, the highest such tax or, as the case may be, such charge.

Additional Levies

Having computed the above mentioned duties, you have to determine whether there are any additional levies on the particular items you intend to import. Some of the levies are commodity specific and would be applicable regardless of the time of

import. These include cesses under various enactments as also Additional Duties on specified commodities.

There are certain other levies which are specific to the country of origin. Consider the following levies—

Countervailing Duty on bounty-fed articles is leviable under Section 9 of the Customs Tariff Act 1975. No such duty is however, being levied at present.

Anti-dumping Duty (Section 9A, Customs Tariff Act, 1975) on specified goods imported from specified countries to protect indigenous industry from injury resulting from dumping of goods. This is notified and published from time to time.

Safeguard Duty (Section 8B of the Customs Tariff Act, 1975) is applicable on certain goods at the time of import for specified periods in order to check their excessive imports which may be injurious to the Indian industry.

Exemptions

The exemptions and concessions can be granted in a number of ways. Some of these exemptions are briefly discussed below:

Exemption by Notification

The Central Government may notify by publication in the Official Gazette certain exemptions and concessions. Such exemptions or concessions may be conditional or absolute. There are general exemptions given to a variety of items imported under certain conditions. These include exemption of imports for promotion of exports, imports by UN bodies, defence imports etc. There are also exemptions which are unconditional and are applicable across the board. There are other exemptions based on conditions of end use.

Preferential Rates

Preferential rates of customs duty have been made applicable in respect of imports from certain countries such as Sri Lanka, Mauritius, Seychelles and Tonga provided certain conditions are satisfied. The goods in question must actually be manufactured or produced in such preferential areas. Rules have been framed in order to determine whether the goods have been manufactured or produced in such areas. Determination of origin of the goods is very essential in order to avail of the benefits of such concessional rates of duty.

To ascertain the applicable rate of duty, refer to the Customs Tariff rates of duties along with exemption notification, if any.

Second Schedule

Very few items are subject to customs duties on their export. For details refer to the Second Schedule and the exemption notifications for exports. However, cesses are leviable on export of several commodities under various Acts.

7.5 VALUATION OF GOODS FOR LEVY OF CUSTOMS DUTY

The method of valuation of goods for both import and export for the purposes of levy of customs duty on the basis of value has been set out under Section 14 of the

Customs Act, 1962. This section has been amended from time to time so as to adhere to international standards.

7.5.1 SECTION 14: VALUATION OF GOODS FOR PURPOSES OF ASSESSMENT

The new valuation Section 14 has been introduced in the budget, 2007.

The following are the details of the new section:

Section 14 of the Customs Act, 1962 was further amended as per the latest amendment, the value of imported and export goods:

Shall be the Transaction Value – that is the price actually paid or payable;

- When sold for export to India;
- For delivery at the time and place of importation in case of imports

and in case of exports it is the price for delivery at the time and place of exportation

- The transaction to be between un-related persons;
- price is to be the sole consideration for the sale subject to such other conditions as “may be specified in the rules” made in this behalf.

The transaction value – price in addition to the price paid or payable on imported goods shall include any amount paid or payable for costs and services including:

- commissions and brokerage,
- engineering,
- design work,
- royalties and license fees,
- costs of transportation to the place of importation,
- insurance,
- loading, unloading and handling charges.

The costs and services required to be included in the price actually paid or payable are exhaustive.

“Loading” and “unloading” charges have also been included along with the “handling charges”.

The rate of exchange shall be as on the date of submission of bill of entry or shipping bill as the case may be.

Section 14(2) permits the BOARD, to fix tariff values for the purpose of valuation. While fixing such values the trend values of such goods shall be considered.

Note: Tariff values have been fixed for crude palm oil, crude soya bean oil, palm oil brass scrap, and poppy seeds.

New Valuation scheme provided for separate rules for imports and exports.

7.5.2 CUSTOMS VALUATION (DETERMINATION OF PRICE OF IMPORTED GOODS) RULES, 2007

As per Notification No. 94/2007-Customs (N.T.), dated 13.9.2007, in exercise of the powers conferred by Section 156 read with Section 14 of the Customs Act, 1962 (62 of 1962), the Central Government hereby makes the following rules, namely:

IMPORTED GOODS

Customs Valuation (Determination of Value of Imported Goods) Rules, 2007

Rule 3	Determination of the method of valuation
Rule 4	Transaction value of identical goods
Rule 5	Transaction value of similar goods
Rule 6	Situation where the above methods can not be applied
Rule 7	Deductive value method
Rule 8	Computed value

(A) SHORT TITLE, COMMENCEMENT AND APPLICATION

(1) These rules may be called the Customs Valuation (Determination of Value of Imported Goods) Rules, 2007.

(2) They shall come into force on the 10th day of October, 2007.

(3) They shall apply to imported goods.

(B) DEFINITIONS

(1) In these rules, unless the context otherwise requires,—

- (a) “computed value” means the value of imported goods determined in accordance with rule 8.
- (b) “deductive value” means the value determined in accordance with rule 7.
- (c) “goods of the same class or kind”, means imported goods that are within a group or range of imported goods produced by a particular industry or industrial sector and includes identical goods or similar goods;
- (d) “identical goods” means imported goods—
 - (i) which are same in all respects, including physical characteristics, quality and reputation as the goods being valued except for minor differences in appearance that do not affect the value of the goods;
 - (ii) produced in the country in which the goods being valued were produced; and
 - (iii) produced by the same person who produced the goods, or where no such goods are available, goods produced by a different person, but shall not include imported goods where engineering, development work, art work, design work, plan or sketch undertaken in India were completed

directly or indirectly by the buyer on these imported goods free of charge or at a reduced cost for use in connection with the production and sale for export of these imported goods;

- (e) “produced” includes grown, manufactured and mined;
- (f) “similar goods” means imported goods—
 - (i) which although not alike in all respects, have like characteristics and like component materials which enable them to perform the same functions and to be commercially interchangeable with the goods being valued having regard to the quality, reputation and the existence of trade mark;
 - (ii) produced in the country in which the goods being valued were produced; and
 - (iii) produced by the same person who produced the goods being valued, or where no such goods are available, goods produced by a different person,

but shall not include imported goods engineering, development work, art work, design work, plan or sketch undertaken in India were completed directly or indirectly by the buyer on these imported goods free of charge or at a reduced cost for use in connection with the production and sale for export of these imported goods;

- (g) “transaction value” means the value referred to in sub-section (1) of section 14 of the Customs Act, 1962;

(2) For the purpose of these rules, persons shall be deemed to be “related” only if—

- (i) they are officers or directors of one another’s businesses;
- (ii) they are legally recognized partners in business;
- (iii) they are employer and employee;
- (iv) any person directly or indirectly owns, controls or holds five per cent or more of the outstanding voting stock or shares of both of them;
- (v) one of them directly or indirectly controls the other;
- (vi) both of them are directly or indirectly controlled by a third person;
- (vii) together they directly or indirectly control a third person; or
- (viii) they are members of the same family.

Explanation I. – The term “person” also includes legal persons.

Explanation II. – Persons who are associated in the business of one another in that one is the sole agent or sole distributor or sole concessionaire, however described, of the other shall be deemed to be related for the purpose of these rules, if they fall within the criteria of this sub-rule.

(C) DETERMINATION OF THE METHOD OF VALUATION (RULE 3)

(1) Subject to rule 12, the value of imported goods shall be the transaction value adjusted in accordance with provisions of rule 10;

(2) Value of imported goods under sub-rule (1) shall be accepted:

Provided that—

- (a) there are no restrictions as to the disposition or use of the goods by the buyer other than restrictions which—
 - (i) are imposed or required by law or by the public authorities in India; or
 - (ii) limit the geographical area in which the goods may be resold; or
 - (iii) do not substantially affect the value of the goods;
- (b) the sale or price is not subject to some condition or consideration for which a value cannot be determined in respect of the goods being valued;
- (c) no part of the proceeds of any subsequent resale, disposal or use of the goods by the buyer will accrue directly or indirectly to the seller, unless an appropriate adjustment can be made in accordance with the provisions of rule 10 of these rules; and
- (d) the buyer and seller are not related, or where the buyer and seller are related, that transaction value is acceptable for customs purposes under the provisions of sub-rule (3) below.

(3) (a) Where the buyer and seller are related, the transaction value shall be accepted provided that the examination of the circumstances of the sale of the imported goods indicate that the relationship did not influence the price.

(b) In a sale between related persons, the transaction value shall be accepted, whenever the importer demonstrates that the declared value of the goods being valued, closely approximates to one of the following values ascertained at or about the same time.

- (i) the transaction value of identical goods, or of similar goods, in sales to unrelated buyers in India;
- (ii) the deductive value for identical goods or similar goods;
- (iii) the computed value for identical goods or similar goods:

Provided that in applying the values used for comparison, due account shall be taken of demonstrated difference in commercial levels, quantity levels, adjustments in accordance with the provisions of rule 10 and cost incurred by the seller in sales in which he and the buyer are not related;

(c) substitute values shall not be established under the provisions of clause (b) of this sub-rule.

(4) If the value cannot be determined under the provisions of sub-rule (1), the value shall be determined by proceeding sequentially through rule 4 to 9.

(D) TRANSACTION VALUE OF IDENTICAL GOODS (RULE 4)

- (1) (a) Subject to the provisions of rule 3, the value of imported goods shall be the transaction value of identical goods sold for export to India and imported at or about the same time as the goods being valued;

Provided that such transaction value shall not be the value of the goods provisionally assessed under section 18 of the Customs Act, 1962.

- (b) In applying this rule, the transaction value of identical goods in a sale at the same commercial level and in substantially the same quantity as the goods being valued shall be used to determine the value of imported goods.
- (c) Where no sale referred to in clause (b) of sub-rule (1), is found, the transaction value of identical goods sold at a different commercial level or in different quantities or both, adjusted to take account of the difference attributable to commercial level or to the quantity or both, shall be used, provided that such adjustments shall be made on the basis of demonstrated evidence which clearly establishes the reasonableness and accuracy of the adjustments, whether such adjustment leads to an increase or decrease in the value.

(2) Where the costs and charges referred to in sub-rule (2) of rule 10 of these rules are included in the transaction value of identical goods, an adjustment shall be made, if there are significant differences in such costs and charges between the goods being valued and the identical goods in question arising from differences in distances and means of transport.

(3) In applying this rule, if more than one transaction value of identical goods is found, the lowest such value shall be used to determine the value of imported goods.

(E) TRANSACTION VALUE OF SIMILAR GOODS (RULE 5)

(1) Subject to the provisions of rule 3, the value of imported goods shall be the transaction value of similar goods sold for export to India and imported at or about the same time as the goods being valued:

Provided that such transaction value shall not be the value of the goods provisionally assessed under section 18 of the Customs Act, 1962.

The provisions of clauses (b) and (c) of sub-rule (1), sub-rule (2) and sub-rule (3), of rule 4 shall, mutates mutandis, also apply in respect of similar goods.

(F) DETERMINATION OF VALUE WHERE VALUE CAN NOT BE DETERMINED UNDER RULES 3, 4 AND 5 (RULE 6)

If the value of imported goods cannot be determined under the provisions of rules 3, 4 and 5, the value shall be determined under the provisions of rule 7 or, when the value cannot be determined under that rule, under rule 8.

Provided that at the request of the importer, and with the approval of the proper officer, the order of application of rules 7 and 8 shall be reversed.

(G) DEDUCTIVE VALUE (RULE 7)

(1) Subject to the provisions of rule 3, if the goods being valued or identical or similar imported goods are sold in India, in the condition as imported at or about the time at which the declaration for determination of value is presented, the value of

imported goods shall be based on the unit price at which the imported goods or identical or similar imported goods are sold in the greatest aggregate quantity to persons who are not related to the sellers in India, subject to the following deductions:

- (i) either the commission usually paid or agreed to be paid or the additions usually made for profits and general expenses in connection with sales in India of imported goods of the same class or kind;
- (ii) the usual costs of transport and insurance and associated costs incurred within India;
- (iii) the customs duties and other taxes payable in India by reason of importation or sale of the goods.

(2) If neither the imported goods nor identical nor similar imported goods are sold at or about the same time of importation of the goods being valued, the value of imported goods shall, subject otherwise to the provisions of sub-rule (1), be based on the unit price at which the imported goods or identical or similar imported goods are sold in India, at the earliest date after importation but before the expiry of ninety days after such importation.

- (3) (a) If neither the imported goods nor identical nor similar imported goods are sold in India in the condition as imported, then, the value shall be based on the unit price at which the imported goods, after further processing,
- (b) In such determination, due allowance shall be made for the value added by processing and the deductions provided for in items (i) to (iii) of sub-rule (1). Computed value

(H) COMPUTED VALUE (RULE 8)

Subject to the provisions of rule 3, the value of imported goods shall be based on a computed value, which shall consist of the sum of:

- (a) the cost or value of materials and fabrication or other processing employed in producing the imported goods;
- (b) an amount for profit and general expenses equal to that usually reflected in sales of goods of the same class or kind as the goods being valued which are made by producers in the country of exportation for export to India;
- (c) the cost or value of all other expenses under sub-rule (2) of rule 10.

(I) RESIDUAL METHOD (RULE 9)

(1) Subject to the provisions of rule 3, where the value of imported goods cannot be determined under the provisions of any of the preceding rules, the value shall be determined using reasonable means consistent with the principles and general provisions of these rules and on the basis of data available in India;

Provided that the value so determined shall not exceed the price at which such or like goods are ordinarily sold or offered for sale for delivery at the time and place of importation in the course of international trade, when the seller or buyer has no

interest in the business of other and price is the sole consideration for the sale or offer for sale.

(2) No value shall be determined under the provisions of this rule on the basis of—

- (i) the selling price in India of the goods produced in India;
- (ii) a system which provides for the acceptance for customs purposes of the highest of the two alternative values;
- (iii) the price of the goods on the domestic market of the country of exportation;
- (iv) the cost of production other than computed values which have been determined for identical or similar goods in accordance with the provisions of rule 8;
- (v) the price of the goods for the export to a country other than India;
- (vi) minimum customs values; or
- (vii) arbitrary or fictitious values.

(J) COST AND SERVICES (RULE 10)

(1) In determining the transaction value, there shall be added to the price actually paid or payable for the imported goods,—

- (a) the following to the extent they are incurred by the buyer but are not included in the price actually paid or payable for the imported goods, namely:-
 - (i) commissions and brokerage, except buying commissions;
 - (ii) the cost of containers which are treated as being one for customs purposes with the goods in question;
 - (iii) the cost of packing whether for labour or materials;
- (b) the value, apportioned as appropriate, of the following goods and services where supplied directly or indirectly by the buyer free of charge or at reduced cost for use in connection with the production and sale for export of imported goods, to the extent that such value has not been included in the price actually paid or payable, namely:-
 - (i) materials, components, parts and similar items incorporated in the imported goods;
 - (ii) tools, dies, moulds and similar items used in the production of the imported goods;
 - (iii) materials consumed in the production of the imported goods;
 - (iv) engineering, development, art work, design work, and plans and sketches undertaken elsewhere than in India and necessary for the production of the imported goods;
- (c) royalties and licence fees related to the imported goods that the buyer is required to pay, directly or indirectly, as a condition of the sale of the goods

being valued, to the extent that such royalties and fees are not included in the price actually paid or payable;

- (d) The value of any part of the proceeds of any subsequent resale, disposal or use of the imported goods that accrues, directly or indirectly, to the seller;
- (e) all other payments actually made or to be made as a condition of sale of the imported goods, by the buyer to the seller, or by the buyer to a third party to satisfy an obligation of the seller to the extent that such payments are not included in the price actually paid or payable.

Explanation: Where the royalty, licence fee or any other payment for a process, whether patented or otherwise, is includible referred to in clauses (c) and (e), such charges shall be added to the price actually paid or payable for the imported goods, notwithstanding the fact that such goods may be subjected to the said process after importation of such goods.

(2) For the purposes of sub-section (1) of section 14 of the Customs Act, 1962 (52 of 1962) and these rules, the value of the imported goods shall be the value of such goods, for delivery at the time and place of importation and shall include—

- (a) the cost of transport of the imported goods to the place of importation;
- (b) loading, unloading and handling charges associated with the delivery of the imported goods at the place of importation; and
- (c) the cost of insurance:

Provided that—

- (i) where the cost of transport referred to in clause (a) is not ascertainable, such cost shall be twenty per cent of the free on board value of the goods;
- (ii) the charges referred to in clause (b) shall be one per cent of the free on board value of the goods plus the cost of transport referred to in clause (a) plus the cost of insurance referred to in clause (c);
- (iii) where the cost referred to in clause (c) is not ascertainable, such cost shall be 1.125% of free on board value of the goods;

Provided further that in the case of goods imported by air, where the cost referred to in clause (a) is ascertainable, such cost shall not exceed twenty per cent of free on board value of the goods:

Provided also that where the free on board value of the goods is not ascertainable, the costs referred to in clause (a) shall be twenty per cent of the free on board value of the goods plus cost of insurance for clause (i) above and the cost referred to in clause (c) shall be 1.125% of the free on board value of the goods plus cost of transport for clause (iii).

Provided also that in case of goods imported by sea stuffed in a container for clearance at an Inland Container Depot or Container Freight Station, the cost of freight incurred in the movement of container from the port of entry to the Inland Container Depot or Container Freight Station shall not be included in the cost of transport referred to in clause (a).

Explanation: The cost of transport of the imported goods referred to in clause (a) includes the ship demurrage charges on chartered vessels, lighterage or barge charges.

(3) Additions to the price actually paid or payable shall be made under this rule on the basis of objective and quantifiable data.

(4) No addition shall be made to the price actually paid or payable in determining the value of the imported goods except as provided for in this rule.

(K) DECLARATION BY THE IMPORTER (RULE 11)

(1) The importer or his agent shall furnish—

- (a) a declaration disclosing full and accurate details relating to the value of imported goods; and
- (b) any other statement, information or document included an invoice of the manufacturer or producer of the imported goods where the goods are imported from or through a person other than the manufacturer or producer, as considered necessary by the proper officer for determination of the value of imported goods under these rules.

(2) Nothing contained in these rules shall be construed as restricting or calling into question the right of the proper officer of customs to satisfy himself as to the truth or accuracy of any statement, information, document or declaration presented for valuation purposes.

(3) The provisions of the Customs Act, 1962 (52 of 1962) relating to confiscation, penalty and prosecution shall apply to cases where wrong declaration, information, statement or documents are furnished under these rules.

(L) REJECTION OF DECLARED VALUE (RULE 12)

(1) When the proper officer has reason to doubt the truth or accuracy of the value declared in relation to any imported goods, he may ask the importer of such goods to furnish further information including documents or other evidence and if, after receiving such further information, or in the absence of a response of such importer, the proper officer still has reasonable doubt about the truth or accuracy of the value so declared, it shall be deemed that the transaction value of such imported goods cannot be determined under the provisions of sub-rule (1) of rule 3.

(2) At the request of an importer, the proper officer, shall intimate the importer in writing the grounds for doubting the truth or accuracy of the value declared in relation to goods imported by such importer and provide a reasonable opportunity of being heard, before taking a final decision under sub-rule (1).

Explanation: (1) For the removal of doubts, it is hereby declared that:

- (i) This rule by itself does not provide a method for determination of value, it provides a mechanism and procedure for rejection of declared value in cases where there is reasonable doubt that the declared value does not represent the transaction value; where the declared value is rejected, the value shall be determined by proceeding sequentially in accordance with rules 4 to 9.

- (ii) The declared value shall be accepted where the proper officer is satisfied about the truth and accuracy of the declared value after the said enquiry in consultation with the importers.
- (iii) The proper officer shall have the powers to raise doubts on the truth or accuracy of the declared value based on certain reasons which may include—
 - (a) the significantly higher value at which identical or similar goods imported at or about the same time in comparable quantities in a comparable commercial transaction were assessed;
 - (b) the sale involves an abnormal discount or abnormal reduction from the ordinary competitive price;
 - (c) the sale involves special discount limited to exclusive agents;
 - (d) the misdeclaration of goods in parameters such as description, quality, quantity, country of origin, year of manufacture or production.

7.6 VALUATION OF EXPORT GOODS

7.6.1 Custom Valuation (Determination of Value of Export Goods) Rules, 2007

As per Notification No. 95/2007-Customs (N.T.) dated 13.9.07, in exercise of the powers conferred by section 156 read with section 14 of the Customs Act, 1962 (52 of 1962) the Central Government hereby makes the following rules, namely,—

(A) Short title, commencement and application

- (1) These rules may be called the Customs Valuation (Determination of Value of Export Goods) Rules, 2007.
- (2) They shall come into force on the 10th day of October, 2007.
- (3) They shall apply to export goods.

(B) Definitions

- (1) In these rules, unless the context otherwise requires,—
 - (a) “goods of like kind and quality” means export goods which are identical or similar in physical characteristics, quality and reputation as the goods being valued, and perform the same functions or are commercially interchangeable with the goods being valued, produced by the same person or a different person; and
 - (b) “transaction value” means the value of export goods within the meaning of sub-section (1) of section 14 of the Customs Act, 1962 (52 of 1962).
- (2) For the purposes of these rules, persons shall be deemed to be “related” only if—
 - (i) they are officers or directors of one another’s businesses;
 - (ii) they are legally recognized partners in business;
 - (iii) they are employer and employee;

- (iv) any person directly or indirectly owns, controls or holds five per cent or more of the outstanding voting stock or shares of both of them;
- (v) one of them directly or indirectly controls the other;
- (vi) both of them are directly or indirectly controlled by a third person;
- (vii) together they directly or indirectly control a third person; or
- (viii) they are members of the same family.

Explanation I: The term "person" also includes legal persons.

Explanation II: Persons who are associated in the business of one another in that one is the sole agent or sole distributor or sole concessionaire, howsoever described, of the other shall be deemed to be related for the purpose of these rules, if they fall within the criteria of this sub-rule.

(C) Determination of the method of valuation (Rule 3)

- (1) Subject to rule 8, the value of export goods shall be the transaction value.
- (2) The transaction value shall be accepted even where the buyer and seller are related, provided that the relationship has not influenced the price.
- (3) If the value cannot be determined under the provisions of sub-rule (1) and sub-rule (2), the value shall be determined by proceeding sequentially through rules 4 to 6.

(D) Determination of export value by comparison (Rule 4)

- (1) The value of the export goods shall be based on the transaction value of goods of like kind and quality exported at or about the same time to other buyers in the same destination country of importation or in its absence another destination country of importation adjusted in accordance with the provisions of sub-rule (2).
- (2) In determination of the value of export goods under sub-rule (1), the proper officer shall make such adjustments as appear to him reasonable, taking into consideration the relevant factors, including—
 - (i) difference in the dates of exportation,
 - (ii) difference in commercial levels and quantity levels,
 - (iii) difference in composition, quality and design between the goods to be assessed and the goods with which they are being compared,
 - (iv) difference in domestic freight and insurance charges depending on the place of exportation.

(E) Computed value method (Rule 5)

If the value cannot be determined under rule 4, it shall be based on a computed value, which shall include the following:

- (a) cost of production, manufacture or processing of export goods;

- (b) charges, if any, for the design or brand;
- (c) an amount towards profit.

(F) Residual method (Rule 6)

(1) Subject to the provisions of rule 3, where the value of the export goods cannot be determined under the provisions of rules 4 and 5, the value shall be determined using reasonable means consistent with the principles and general provisions of these rules provided that local market price of the export goods may not be the only basis for determining the value of export goods.

(G) Declaration by the exporter (Rule 7)

The exporter shall furnish a declaration relating to the value of export goods in the manner specified in this behalf.

(H) Rejection of declared value (Rule 8)

(1) When the proper officer has reason to doubt the truth or accuracy of the value declared in relation to any export goods, he may ask the exporter of such goods to furnish further information including documents or other evidence and if, after receiving such further information, or in the absence of a response of such exporter, the proper officer still has reasonable doubt about the truth or accuracy of the value so declared, the transaction value shall be deemed to have not been determined in accordance with sub-rule (1) of rule 3.

(2) At the request of an exporter, the proper officer shall intimate the exporter in writing the ground for doubting the truth or accuracy of the value declared in relation to the export goods by such exporter and provide a reasonable opportunity of being heard, before taking a final decision under sub-rule (1).

Explanation: (1) For the removal of doubts, it is hereby declared that—

- (i) This rule by itself does not provide a method for determination of value, it provides a mechanism and procedure for rejection of declared value in cases where there is reasonable doubt that the declared value does not represent the transaction value; where the declared value is rejected, the value shall be determined by proceeding sequentially in accordance with rules 4 to 6.
- (ii) The declared value shall be accepted where the proper officer is satisfied about the truth or accuracy of the declared value after the said enquiry in consultation with the exporter.
- (iii) The proper officer shall have the powers to raise doubts on the declared value based on certain reasons which may include—
 - (a) the significant variation in value at which goods of like kind and quality exported at or about the same time in comparable quantities in a comparable commercial transaction were assessed.
 - (b) the significantly higher value compared to the market value of goods of like kind and quality at the time of export.

- (c) the misdeclaration of goods in parameters such as description, quality, quantity, year of manufacture or production.

Practical illustrations (Customs Valuation)

Question: CIF value: 10,000 US Dollars

Exchange rate notified by RBI: ₹ 46/-

Exchange rate notified by CBEC: ₹ 45/-

The following rates of customs are applicable to the consignment

- (1) Basic customs duty: 10%
- (2) CVD 16%. Same goods manufactured in India attract exemption by 6%
- (3) Education cess is payable at (Assumed)2%.
- (4) Special CVD is payable at applicable rates.

Find out:

- (i) Assessable value
- (ii) Duties payable
- (iii) Eligibility of CENVAT Credit

Solution

CIF Value	10,000	USD
Add: Landing charges @ 1% of CIF Value	<u>100</u>	
Assessable value	10,100	USD
₹ 45 x 10,100 = 4,54,500		
	₹	Duty (₹)
Assessable Value	4,54,500	
(1) Add: B.C.D. @10%	<u>45,450</u>	45,450
	4,99,950	
(2) Add: CVD @10% (16% – 6%)	<u>49,995</u>	49,995
	5,49,945	
(3) Add: Edu. Cess @2% on ₹ 49,995	<u>1,000</u>	1,000
	5,50,945	96,445
(4) Add: Edu. Cess @2% on total duty on customs i.e. on 96,445	<u>1,929</u>	1,929
Total Value for adding Spl. CVD	5,52,874	98,374
Add: Spl. CVD @4% on 5,52,874	<u>22,115</u>	<u>22,115</u>
Total	<u>5,74,989</u>	<u>1,20,489</u>

Total CENVAT Credit available to the buyer is

₹ 49,995 + ₹ 1,000 + ₹ 22,115 = ₹ 73,100

Question: Find the assessable value.

Import by Air

CIF Value: 1,000 Euros.

Freight: 300 Euros

Insurance: 15 Euros

The exchange rate notified by CBEC as on the date of submission of Bill of Entry was ₹ 50 per euro.

Solution

Since the freight charges cannot exceed 20% of FOB value, it is necessary to find out FOB value.

	Euros	
FOB value:		1,000
Less: Freight	300	
Insurance	<u>15</u>	
FOB	315	
Add: Freight @20% on 685	137	
Add: Insurance	<u>15</u>	837.00
Add: Landing charges @1%		<u>8.37</u>
		<u>845.37</u>

Assessable value in Indian Rupees = ₹ 50 x 845.37 = ₹ 42,269/- (rounded off)

7.7 Determination of Rate of Duty and Tariff Valuation

In any Taxation law, quantification of the tax liability is the most important function. This quantification in the case of goods attracting *ad-valorem* rates of duties depends upon two variables. One the value of the goods and two the rate of duty applicable. Once the value is decided and the rate of duty is also ascertained, quantification becomes easier. But the crucial question is what is the date on which valuation of such goods is to be made and the rate applicable thereto. Section 15 of the Act deals with this important aspect. This runs as follows:

(A) Date for determination of rate of duty and tariff valuation of imported goods

(1) The rate of duty and tariff valuation if any, applicable to any imported goods, shall be the rate and valuation in force:

- (a) in the case of goods entered for home consumption under Section 46, on the date on which a bill of entry in respect of such goods is presented under that section;
- (b) in the case of goods cleared from a warehouse under Section 68, on the date on which a bill of entry for home consumption in respect of such goods is presented under that section.
- (c) in the case of any other goods, on the date of payment of duty.

Provided that if a bill of entry has been presented before the date of entry inwards of the vessel or the arrival of the aircraft by which the goods are imported, the bill of entry shall be deemed to have been presented on the date of such entry inwards or the arrival, as the case may be.

(2) The provisions of this section shall not apply to baggage and goods imported by post”.

Case Laws:



1. In *Pan Asia Commercial Enterprises and Another v. Union of India* 1986 (25) ELT 508 (Bom.), it has been held that Section 3 of the Customs Tariff Act makes it clear that additional duty cannot be levied on an article imported into India, if such article manufactured in India is exempt from payment of Excise duty. Hence, liability to countervailing (additional) duty would depend on the liability to pay Excise duty. The fact that the articles are not liable to pay excise duty will have a bearing on determination of the liability to pay countervailing duty.

2. In *Hyderabad Industries Ltd. v. U.O.I.* 1999 (108) ELT, The S.C. held that additional duty can be levied only if such article imported is as a result of manufacture in India. The asbestos fibre imported is not manufacture as the fibre is same as the parent rock. Hence, no CVD on the fibre imported.

(B) Date for determination of the rate of duty and tariff valuation of export goods

Section 16 deals with this. Accordingly, the rate of duty and tariff valuation, if any, applicable to any export goods, shall be the rate and valuation in force:

- (a) in the case of goods entered for export under Section 50, on the date on which the proper officer makes an order permitting clearance and loading of the goods for exportation under Section 51;
- (b) in the case of any other goods, on the date of payment of duty;

Provided that if the shipping bill has been presented before the date of entry outwards of the vessel by which the goods are to be exported, the shipping bill shall be deemed to have been presented on the date of such entry outwards and the relevant date would be the date of entry outwards.

In *Collector of Customs, Cochin v. M.S.P. Exports, Mangalore* [1986 (26) ELT 848 (Trib.)], it was held that where the shipping bill was originally presented on 25.8.1981 and the entry outward granted on 12.9.1981, then under the deeming provision of Section 16, the date of presentation of the shipping bill should be 12.9.1981 only. Since duty was paid on 25.8.1981 and the rate of duty would be the rate prevalent on 12.9.1981 but by 10.9.1981 duty on export goods in the case stood abolished, no duty was payable by the respondent on their exports.

In case of export by land, the rate of duty applicable to such goods shall be the rate and valuation in force when the application for permit to export is made.

Relevant date in case of amended Shipping Bills — If an amendment in the shipping bill is allowed and the fresh bill is filed after withdrawal of the original, the provisions of Section 16(1) would apply to the bill so presented. Where the shipping

bill was presented on 16.6.1981 after the date of entry outward for the vessel was given but the shipping bill was amended on 19.6.1981, it was held that under Section 16 the duty should have been as on 19.6.1981 i.e. NIL rate of duty and therefore, the refund claim was admissible to the exporter [*Collector of Customs, Cochin v. Ramesh Enterprises (Pvt.) Ltd. Bangalore - 1987 (31) ELT 549 (Trib.)*].

These provisions shall not apply to baggage and goods exported by post.

(C) Determination of duty in case of Articles liable to different rates of duty

Section 19 of the Act lays down the authority for determining of duty where goods consist of a set of articles liable to different rates of duty. The section reads as follows:

Determination of duty where goods consist of articles liable to different rates of duty: Except as otherwise provided in any law for the time being in force, where goods consist of a set of articles, duty shall be calculated as follows:

- (a) articles liable to duty with reference to quantity shall be chargeable to that duty;
- (b) articles liable to duty with reference to value shall, if they are liable to duty at the same rate, be chargeable to duty at that rate, and if they are liable to duty at different rates, be chargeable to duty at the highest of such rates;
- (c) articles not liable to duty shall be chargeable to duty at the rate at which articles liable to duty with reference to value are liable under clause (b).

Provided that —

- (a) accessories of, and spare parts or maintenance and repairing implements for, any article which satisfy the conditions specified in the rules made in this behalf shall be chargeable at the same rate of duty as that article;
- (b) if the importer produces evidence to the satisfaction of the proper officer or the evidence is available regarding the value of any of the articles liable to different rates of duty, such article shall be chargeable to duty separately at the rate applicable to it.

The section embodies the principle that where a part or ingredient of an article is liable to duty though the entire article as such may not be liable, the goods may be taxed as if they had been entirely composed of such dutiable articles. It provides for levy of duty on composite products or commodities made up of more than one material, the end product of a mixture or corresponding articles where the end product or mixture itself is a specifically identifiable commodity having an individuality of its own differing from its components. As observed in *S.S. Navigation Co. v. Union of India*, [AIR (1968) Madras 289], goods contemplated under this section are those which are made up of more than one article which cannot be separated into their components or divided off into their constituents without destroying the specific quality or individually they had acquired as composite goods.

7.8 Remission, Exemption and Demands in Customs:

7.8.1 Duty on Pilfered Goods

Section 13 provides that if any goods are pilfered after the unloading thereof and before the proper officer has made an order for clearance for home

consumption or deposit in a warehouse, the importer shall not be liable to pay the duty leviable on such goods except where such goods are restored to the importer after pilferage.

Under the section, duty is not payable on pilfered goods only in cases where the goods are pilfered after the unloading and before the customs authorities issue the order for clearance. If, therefore, the goods are pilfered after the order of clearance is made but before they are actually cleared, duty is leviable. This section, however, concerns itself with only pilferage of goods but not with loss or destruction which are covered under Section 23 of the Customs Act. The reason is that if the goods have already been lost or destroyed, no bill of lading in relation to such goods is likely to be filed which is only done in case the goods are in existence and are tendered for assessment.

Further, from the Scheme of the Act, it is clear that the situation contemplated under this section is prior to assessment and therefore, the importer is not made liable to pay the duty on the imported goods which are pilfered after unloading but before the proper officer has made an order for clearance for home consumption except where such goods are restored to him. Therefore, in such a situation, if the duty has already been paid the importer is eligible for refund of such duty paid on the pilfered quantity. As such the situation contemplated under Section 13 is not necessarily and inevitably prior to the assessment which could be done in two ways; one is to examine the goods, test them, if necessary, then assess the duty thereon, collect the duty and make the out-of-charge order; two, to assess the duty on goods on the basis of documents presented by the importer, collect the duty, then examine the goods for verifying the correctness of the assessment and thereafter make out-of-charge order [*Hindustan Petroleum Corporation Ltd. v. Collector of Customs, Bombay* 1984 (18) ECT 358 (Trib.)], However, the sum and substance of Section 13 is that pilferage ought to be detected before order for clearance of goods is given irrespective of whether duty has been paid or not. In *Bharat Earth Movers Ltd., Madras v. Collector of Customs, Madras*, 1985 (20) ELT 163 (Trib.), where the relevant Bill of Entry was presented, assessed and duty paid prior to the arrival of the vessel as also order for clearance of goods given by the proper officer before examination of consignment and detection of the shortage in goods, it was held that refund is barred under Section 13 and it is not open to the importer to claim that he is pre-judged by the action and should be protected against it or that the goods might not have been landed, or could have been lost and hence not available for examination is not sufficient to establish a claim for refund.

7.8.2 Re-Importation of Goods

When goods are re-imported into India, after exportation there from, such goods are liable to duty and are subject to all the conditions and restrictions, if any, to which goods of the like kind and value are liable or subject, on the importation thereof. The provisions relating to these matters are found in Section 20 of the Customs Act, 1962.

Section 20, which got amended by Finance Act, 1994, (w.e.f. 13.5.1994), until this amendment, covered only goods produced and manufactured in India, when imported after being exported from India and provided that these will be chargeable to customs duty and subject to the same conditions as goods imported afresh. However, the amendment has extended the applicability of the provisions of this

section to all goods imported into India after being exported and not only those goods which are manufactured or produced in India. Thus, goods imported after being exported in bond would henceforth be chargeable to normal customs duty. The amended Section 20 reads as under:

If goods are imported into India after exportation there from, such goods shall be liable to duty and be subject to all the conditions and restrictions, if any, to which goods of the like kind and value are liable or subject, on the importation thereof.

Notification Nos. 94/96 and 158/95 provide for certain relaxations for reimported goods.

7.8.3 Goods derelict, wreck etc.

Section 21 lays down that all goods, derelict, jetsam, flotsam and wreck brought or coming into India, shall be dealt with as if they were imported into India, unless it be shown to the satisfaction of the proper officer that they are entitled to be admitted duty free under this Act.

“Derelict” is a term applied to any property, whether vessel or cargo, left or abandoned in open sea by persons in charge of it without any hope of recovering or intention of returning to it.

“Jetsam” is where the goods are thrown into the sea with a view to lighten the ship in order to prevent it from sinking.

“Flotsam” is where the goods having been at sea in a ship, are separated from it by some peril. The property in this case is not renounced by the owner by throwing them overboard and the owner is entitled to recover the possession.

“Wreck” refers to the property cast ashore within the ebb and flow of the tide after shipwreck. The property involved may be a ship, a cargo or portion thereof.

7.8.4 Abatement of Duty

If any goods are found damaged and are examined by customs authority for that purpose on an application made therefor, the duty can be charged only on the goods which are serviceable or on the reduced value as may be determined by customs authority. Provisions in this regard have been made under Section 22 of the Customs Act, 1962.

Under Section 22, there is allowed abatement of duty on damaged or deteriorated goods under Sub-section (1), where it is shown to the satisfaction of the Assistant/Deputy Commissioner of Customs—

- (a) that any imported goods had been damaged or had deteriorated at any time before or during the unloading of the goods in India; or
- (b) that any imported goods, other than warehoused goods, had been damaged at any time after the unloading thereof in India but before their examination under Section 17, on account of any accident not due to any wilful act, negligence or default of the importer, his employee or agent; or
- (c) that any warehoused goods have been damaged at any time before clearance for home consumption on account of any accident not due to any wilful act, negligence or default of the owner his employee or agent.

Such goods are chargeable to duty in accordance with the provisions of Sub-section (2).

Sub-section (2) lays down that the duty to be charged on the goods referred above shall bear the same proportion to the duty chargeable on the goods before the damage or deterioration which the value of the damaged or deteriorated goods bear to the value of the goods before the damage or deterioration.

Under Sub-section (3), the value of damaged or deteriorated goods may, be ascertained by either of the following methods at the option of the owner, viz.:

- (a) the value of such goods may be ascertained by the proper officer, or
- (b) such goods may be sold by the proper officer by public auction or by tender, or with the consent of the owner in any other manner and the gross proceeds shall be deemed to be the value of such goods.

7.8.5 Remission of duty on lost, destroyed or abandoned goods (Section 23)

Where any goods are lost or destroyed, except by way of pilferage, whether totally or partially, even after the "out of charge" is signed but before they are physically removed from customs area, the owner is entitled for remission of duty on such goods.

Further, an owner of goods can surrender the title to the goods to customs before an order for home consumption has been made and no duty need be paid on such goods.

Section 23 relates to remission of duty on lost, destroyed or abandoned goods. It reads as follows:

- (1) Without prejudice to the provisions of Section 13, where it is shown to the satisfaction of the Assistant/Deputy Commissioner of Customs that any imported goods have been lost otherwise than as a result of pilferage or destroyed, at any time before clearance for home consumption, the Assistant/Deputy Commissioner of Customs shall remit the duty on such goods.
- (2) The owner of any imported goods may, at any time before an order for clearance of goods for home consumption under Section 47 or an order for permitting the deposit of goods in a warehouse under Section 60 has been made, relinquish his title to the goods and thereupon he shall not be liable to pay the duty thereon".

Provided that the owner of any such imported goods shall not be allowed to relinquish his title to such goods regarding which an offence appears to have been committed under this Act or any other law for the time being in force.

7.8.6 Denaturing or Mutilation of Goods (Section 24)

Where any goods attract a higher rate of duty, in the condition in which they are imported e.g. pure alcohol, Brass articles, wearing apparels, but could be charged to duty at a lower rate if their nature is different such as denatured, unserviceable brass scraps, rags etc., Section 24 authorises change in the form of such goods to the

other form and charging of lower rate of duty attracted by goods in changed form. For this purpose, a request has to be made by the owners for denaturing or mutilation, as the case may be, and carry out such process under customs supervision. If the same is approved, the description and the classification will be suitably amended by the assessing officer and documents completed as usual. New Act as applicable to denatured/mutilated goods be taken for assessment.

7.8.7 Exemption from Duty

The power to grant exemption from duty in respect of any goods liable to Customs duty is found in Section 25 of the Act. This section reads as follows:

- (1) If the Central Government is satisfied that it is necessary in the public interest so to do, it may, by notification in the Official Gazette, exempt generally either absolutely or subject to such conditions (to be fulfilled before or after clearance) as may be specified in the notification, goods of any specified description from the whole or any part of duty of customs leviable thereon.
- * (2) If the Central Government is satisfied that it is necessary in the public interest so to do, it may, by special order in each case, exempt from the payment of duty under circumstances of an exceptional nature to be stated in such order, any goods on which duty is leviable.
- (2A) The Central Government may, if it considers it necessary or expedient so to do for the purpose of clarifying the scope or applicability of any notification issued under Sub-section (1) or order under Sub-section (2), and every such explanation shall have effect as if it had always been the part of the first such notification or order, as the case may be.
- (3) An exemption under Sub-section (1) or Sub-section (2) in respect of any goods from any part of the duty of customs leviable thereon (the duty of customs leviable thereon being hereinafter referred to as the statutory duty) may be granted by providing for the levy of a duty on such goods at a rate expressed in a form or method different from the form or method in which the statutory duty is leviable and any exemption granted in relation to any goods in the manner provided in this subsection shall have effect subject to the condition that the duty of customs chargeable on such goods shall in no case exceed the statutory duty.
Explanation: "Form or method", in relation to a rate of duty of customs, means the basis, namely, valuation, weight, number, length, area, volume or other measure with reference to which the duty is leviable.
- (4) Every notification issued under Sub-section (1) or (2A) shall:
 - (a) unless otherwise provided, come into force on the date of its issue by the Central Government for publication in the Official Gazette;
 - (b) also be published and offered for sale on the date of its issue by the Directorate of Publicity and Public Relations of the Board, New Delhi.

* Inserted by Financial Act, 2003

- (5) Notwithstanding anything contained in Sub-section (4), where a notification comes into force on a date later than the date of its issue, the same shall be published and offered for sale by the said Directorate of Publicity and Public Relations on a date on or before the date on which the said notification comes into force.”
- * (6) Notwithstanding any thing contained in this Act, no duty shall be collected if the amount of duty leviable is equal to, or less than, one hundred rupees.

Under the section, exemptions are of two kinds. One type which is in common use, is under Sub-section (1), in public interest, where there is a general exemption in respect of any article or class of articles. Such exemptions may be absolute or subject to certain conditions specified in the relevant notifications. Under Sub-section (2), the exemptions granted may be applicable to specific cases and these will be by a special order. These have to be done in respect of any goods of strategic or secret nature or for charitable purpose, which are stated in such order.

Notifications exempting goods under Sub-section (1) have to be laid before Parliament, as soon as may be, after their issue and the Parliament may amend or reject them. This shows that such notifications are in exercise of 'sovereignty' i.e. legislative powers. On the other hand, special order under Sub-section (2) is an executive order because it is not required to be published and it grants exemption specifically and not generally.

Sub-sections (4) and (5), puts it beyond doubt that every exemption notification shall, unless otherwise provided, come into force on the date of its issue by the Central Government for publication in the Official Gazette. It is also provided that there shall be a statutory obligation for publication of notifications by the Directorate of Publicity and Public Relations and for their sale to the public. The Directorate of Publicity and Public Relations is required to publish the notifications on the date on which the notification is issued by the Government. If, however, the notification is issued but Public Relations can publish the notification on a date not later than the date from which the notification is to be effective. The notifications shall however, also continue to be published in the Gazette of India, as usual.

This amendment has been made in order to do away with the practical problem caused about effective date of notifications by recent Supreme Court judgement in *Collectors v. New Tobacco Co.* (1998) 97 E.L.T. 388 (S.C.).

However, exemptions granted under Section 25(1) of the Customs Act, can operate only in respect of such duty as is specifically mentioned in the particular notification. Thus, a notification exempting goods from the levy of basic customs duty can not by itself exempt such goods from the levy of countervailing duty or additional duty leviable under the Tariff Act nor can exemption from levy of countervailing duty or additional duty, wholly or partially, result in exemption of the goods from the levy of basic customs duty, wholly or partially.

In order to obtain a keen insight and to understand the philosophy or rationale underlying the grant of exemptions it is pertinent to note the explanation given by the Ministry of Finance to the Public Accounts Committee of the Lok Sabha, which had made some observations regarding manner and reasons underlying grant of exemptions from customs duty [PAC (5th Lok Sabha) (1974-75), 135th Report p. 55]. The Ministry of Finance had explained that the exemptions from customs duty were

granted for one or more of the following reasons:

- (i) in accordance with the General Agreement on Trade and Tariff certain concessions agreed to by India have to be implemented through exemption notifications;
- (ii) in cases, where indigenously manufactured finished products using imported raw materials are placed at a disadvantageous position vis-a-vis imported finished products on account of high incidence of import duties leviable on imported articles, the industries concerned have to be given tariff assistance by bringing down, through exemption notifications, the import duties applicable in the case of imported raw materials to a level necessary for the removal of the disadvantages;
- (iii) in cases where component/raw materials required for the initial setting up, assembly or manufacture of machinery/finished product are assessable to duty at a higher rate than what is leviable on the machinery/finished product, the tariff anomaly has to be set right through exemption notifications, equalising the two rates;
- (iv) certain raw materials/semi-finished products are imported for producing finished products which are to be exported later. In such cases, exemptions from import duties have to be given in the interest of export promotion; and
- (v) some exemptions have to be given on humanitarian grounds like relief, rehabilitation, and repatriation of Indians, etc.

Accordingly, exemptions of the types enumerated above are given under Section 25(1) of the Customs Act, 1962. Ad hoc exemptions, however, are given under Sub-section (2) of the said section only under the designed conditions after the amendment of this sub-section by the Finance Act, 1999. The amended policy guidelines issued by the Finance Ministry for grant of such exemption are reproduced below:

7.8.8 Policy Guidelines for ad hoc exemptions under Section 25(2)

In supersession of the Office Memorandum dated 8th October, 1996, the Finance Minister has approved the following guidelines for consideration of request for exemption from customs duty under Section 25(2) of the Customs Act, 1962 as amended by the Finance Act, 1999:

- (a) Imports of secret goods by Government.
- (b) Imports for India's defence needs relating only to military hardware and software or for R&D units under the DRDO may be allowed free of duty.
- (c) Imports by Central Policy Organisation for equipping their forces may be allowed free of duty.
- (d) State Police Organisations may be allowed to import free of duty equipments required for anti-subversion, anti-terrorism and intelligence work.
- (e) Imports by Charitable Institutions which are providing all their services free where the imports are required for use in hospitals, educational institutions, etc., may be allowed free of duty.

The imports by these charitable organisations should fulfill the following conditions:

- (i) The imports should be received as donations or gifts and the donor should be known institution, but not an individual, say a society or a foundation. No payment for imports should be involved.
- (ii) The recipient should also be an institution/organisation, but not an individual, which is registered as charitable organisation.
- (iii) The said organisation/institution should be providing services, such as running hospitals, educational institutions etc., on either 'free' or 'no loss or no profit' basis.
- (iv) The charitable nature of the organisation and the fact of rendering services on 'free' or 'no loss no profit' basis should be certified by the concerned district authorities.
- (v) The organisation/institution should certify that the goods under import are for its use and provide an undertaking to the effect that they would fulfill the conditions.

2. All ad hoc exemptions from duty to non-governmental organisation will be issued subject to the conditions that the imported goods will not be put to any commercial use and will not be sold, gifted or parted by the importer in any manner without the prior permission of the Ministry of Finance. The imported goods will be kept available for inspection by Customs Officers.

3. Import of goods which are not covered in any of the categories mentioned in para 1 will not be considered for grant of ad hoc exemptions under Section 25(2) of the Customs Act, 1962.

7.8.9 Refund of Duties

Section 26 relates to refund of export duty in certain cases. It reads as follows:

Where on the exportation of any goods any duty has been paid, such duty shall be refunded to the person by whom or on whose behalf it was paid, if:

- (a) the goods are returned to such person otherwise than by way of resale;
- (b) the goods are re-imported within one year from the date of exportation; and
- (c) an application for refund of such duty is made before the expiry of six months from the date on which the proper officer makes an order for the clearance of the goods".

Accordingly, the section permits the refund of export duty if the goods are returned to the exporter within one year from the date of exportation.

Section 26A has been introduced by the Finance Act, 2009 for providing refund of import duty in certain cases.

As per sub section (1) where on the importation of any goods capable of being easily identified as such imported goods, any duty has been paid on clearance of such goods for home consumption, such duty shall be refunded to the person by whom or on whose behalf it was paid, if –

- (a) the goods are found to be defective or otherwise not in conformity with the specifications agreed upon between the importer and the supplier of goods :

Provided that the goods have not been worked, repaired or used after importation except where such use was indispensable to discover the defects or non-conformity with the specifications;

- (b) the goods are identified to the satisfaction of the Assistant Commissioner or Deputy Commissioner of Customs as the goods which were imported;
- (c) the importer does not claim drawback under any other provisions of this Act; and
- (d) (i) the goods are exported ; or (ii) the importer relinquishes his title to the goods and abandons them to customs; or (iii) such goods are destroyed or rendered commercially valueless in the presence of the proper officer,

in such a manner as may be prescribed and within a period not exceeding 30 days from the date on which the proper officer makes an order for the clearance of imported goods for home consumption under section 47.

Provided that the period of 30 days may, on sufficient cause being shown, be extended by the Commissioner for a period not exceeding three months;

Provided further that nothing contained in this section shall apply to the goods regarding which an offence appears to have been committed under this Act or any other law for the time being in force.

(2) An application for refund of duty shall be made before expiry of six months from the relevant date in such form and manner as may be prescribed.

Explanation: For the purpose of this sub-section, 'relevant date' means –

- (a) in cases where the goods are exported out of India , the date on which the proper officer makes an order permitting clearance and loading of goods for exportation under section 51;
- (b) in cases where the title to the goods is relinquished, the date of such relinquishment;
- (c) in cases where the goods are destroyed or rendered commercially valueless, the date of such destruction or rendering of goods commercially valueless.

(3) No refund under sub section (1) shall be allowed in respect of perishable goods and goods which have exceeded their shelf life or their recommended storage-before-use period.

(4) The Board may by notification in the Official Gazette, specify any other condition subject to which the refund may be allowed.

(A) Claim for Refund

(1) Section 27 of the Customs Act deals with the refund of the duty. As per this section—

- (a) Any person who has paid the duty or interest or who has borne the incidence of duty or interest can claim refund of duty by way of application.

- (b) The application for refund is to be made to the Assistant Commissioner of customs or Deputy Commissioner of customs.
- (c) The application should be made before the expiry of one year from the date of payment of such duty or interest. However the limitation period of one year shall not apply where duty or interest is paid under protest.
- (d) The application should be accompanied by such documentary or other evidence to establish that the amount of duty or interest in relation to which such refund is claimed was collected from, or paid by him and incidence of such amount is not transferred to any other person.

The period of one year shall be computed from the following date:

- | | | |
|--|---|--|
| (1) <i>Where goods are exempt from payment of duty by a special order under Sub-section (2) of Section 25</i> | — | <i>Date of issue of such order.</i> |
| (2) <i>Duty becomes refundable because of judgement, decree, order or direction of appellate authority, appellate tribunal, or court</i> | — | <i>Date of such judgement decree, order or direction</i> |
| (3) <i>Duty is paid provisionally under Section 18</i> | — | <i>Date of adjustment of duty after final assessment</i> |

(2) If, on receipt of any such application, the Assistant/Deputy Commissioner of Customs is satisfied that the whole or any part of the duty and interest, if any, paid on such duty paid by the applicant is refundable, he may make an order accordingly and the amount so determined shall be credited to the Fund:

Provided that the amount of duty and interest, if any, paid on such duty as determined by the Assistant/Deputy Commissioner of Customs under the foregoing provisions of this sub-section shall, instead of being credited to the Fund, be paid to the applicant, if such amount is relatable to:

- (a) the duty and interest, if any, paid on such duty paid by the importer or exporter, as the case may be, if he had not passed on the incidence of such duty and interest, if any, paid on such duty to any other person;
- (b) the duty and interest, if any, paid on such duty on imports made by an individual for his personal use;
- (c) the duty and interest, if any, paid on such duty borne by the buyer, if he had not passed on the incidence of such duty and interest, if any, paid on such duty to any other person;
- (d) the export duty as specified in Section 26;
- (e) drawback of duty payable under Sections 74 and 75;

- (f) the duty and interest if any, paid on such duty borne by any other such class of applicants as the Central Government may, by notification in the Official Gazette, specify:

Provided further that no notification under clause (f) of the first proviso shall be issued unless in the opinion of the Central Government the incidence of duty and interest, if any, paid on such duty has not been passed on by the persons concerned to any other person.

(3) Notwithstanding anything to the contrary contained in any judgement, decree, order or direction of the Appellate Tribunal or any Court or in any other provision of this Act or the regulations made thereunder or any other law for the time being in force, no refund shall be made except as provided in Sub-section (2).

(4) Every notification under clause (f) of the first proviso to Sub-section (2) shall be laid before each House of Parliament, if it is sitting, as soon as may be after the issue of the notification, and if it is not sitting, within seven days of its re-assembly, and the Central Government shall seek the approval of Parliament to the notification by a resolution moved within a period of fifteen days beginning with the day on which the notification is so laid before the House of the People and if Parliament makes any modification in the notification or directs that the notification should cease to have effect, the notification shall thereafter have effect only in such modified form or be of no effect, as the case may be, but without prejudice to the validity of anything previously done thereunder.

(5) For the removal of doubts, it is hereby declared that any notification issued under clause (f) of the first proviso to Sub-section (2), including any such notification approved or modified under Sub-section (4), may be rescinded by the Central Government at any time by notification in the Official Gazette.

(B) Interest on delayed refunds

Section 27A incorporated in the Customs Act by the Finance Act, 1995 (w.e.f. 26.5.95) provide for payment of interest on refunds of duty which is not paid to the applicant within three months from the date of receipt of application under Sub-section (1) of Section 27.

It has also been provided that in case where appellate remedies are resorted to either by the Department or by the assessee, the refund finally payable shall bear interest for the period starting from the date immediately after the expiry of three months from the date of receipt of applications under Sub-section (1) of Section 27 till the date of refund of duty. It may be specifically noted that:

- (a) interest will be paid only on the amount of duty which is finally held to be refunded. For example, in case the assessee has claimed a refund of ₹ 60,000/- the Assistant/Deputy Commissioner allows a refund of ₹ 10,000/- and on appeal the amount decided to be refunded is ₹ 30,000/- then the interest would be payable on the amount finally decided to be refunded viz. ₹ 30,000/- for the period commencing from the expiry of three months from the date of the refund application till its payment. Conversely, if the Assistant/Deputy Commissioner has determined the amount due as refund at ₹ 30,000/- which on appeal by the Department is reduced to ₹ 10,000/- interest would be payable for the aforesaid period only on the amount of ₹ 10,000/-;

- (b) the interest will be paid at the rate to be fixed by the Central Government by issue of Gazette Notification as simple interest, Interest on interest is not payable;
- (c) no interest is to be paid on any refund of fines or penalties; the provision has been made for payment of interest only on delayed refund of duty amounts;
- (d) it is to be clearly noted that interest if any would be payable on the amount of duty to be refunded arising only from proceedings initiated under Section 27 i.e. where an application for refund has been filed.

Section 27A reads thus:

If any duty ordered to be refunded under Sub-section (2) of Section 27 to an applicant is not refunded within three months from the date of receipt of application under Sub-section (1) of that section, there shall be paid to that applicant interest at such rate, not below five per cent, and not exceeding thirty per cent per annum as is for the time being fixed by the Central Government by notification in the Official Gazette, on such duty from the date immediately after the expiry of three months from the date of receipt of such application till the date of refund of such duty: Applicable rate of interest is 6% per annum.

Provided that where any duty, ordered to be refunded under Sub-section (2) of Section 27 in respect of an application under Sub-section (1) of that section made before the date on which the Finance Bill, 1995 receives the assent of the President, is not refunded within three months from such date, there shall be paid to the applicant interest under this section from the date immediately after three months from such date till the date of refund of such duty.

Explanation — Where any order of refund is made by Commissioner (Appeals), Appellate Tribunal or any Court against an order of the Assistant/Deputy Commissioner of Customs under Sub-section (2) of Section 27, the order passed by the Commissioner (Appeals), Appellate Tribunal or as the case may be, by the Court, shall be deemed to be an order passed under the sub-section for the purposes of this section.”

When refund becomes payable on account of order by an appellate authority, court or tribunal, the application for refund shall be filed within one year from the date of such order.

7.9 Recovery of Duties

(A) Duties collected from the buyer to be deposited with the Central Government (Section 28B)

(1) Notwithstanding anything to the contrary contained in any order or direction of the Appellate Tribunal or any Court or in any other provision of this Act or the regulations made there under, every person who is liable to pay duty under this Act and has collected any amount in excess of the duty assessed or determined or paid on any goods under this Act from the buyer of such goods in any manner as representing duty of customs, shall forthwith pay the amount so collected to the credit of the Central Government.

(1A) Every person who has collected any amount in excess of the duty assessed or determined or paid on any goods or has collected any amount as representing duty of customs on any goods which are wholly exempt or are chargeable to *nil* rate of duty from any person in any manner, shall forthwith pay the amount so collected to the credit of the Central Government.

(2) Where any amount is required to be paid to the credit of the Central Government under sub-section (1) or sub-section (1A), as the case may be, and which has not been so paid, the proper officer may serve on the person liable to pay such amount, a notice requiring him to show cause why he should not pay the amount, as specified in the notice to the credit of the Central Government.

(3) The proper officer shall, after considering the representation, if any, made by the person on whom the notice is served under Sub-section (2), determine the amount due from such person (not being in excess of the amount specified in the notice) and thereupon such person shall pay the amount so determined.

(4) The amount paid to the credit of the Central Government under Sub-section (1) or sub-section (1A) or Sub-section (3) shall be adjusted against the duty payable by the person on finalisation of assessment of any other proceeding for determination of the duty relating to the goods referred to in Sub-section (1) or Sub-section (1A).

(5) Where any surplus is left after the adjustment made under Sub-section (4), the amount of such surplus shall either be credited to the Fund or, as the case may be, refunded to the person who has borne the incidence of such amount, in accordance with the provisions of Section 27 and such person may make an application under that section in such cases within six months from the date of the public notice to be issued by the Assistant Commissioner of Customs for the refund of such surplus amount.

Section 28BA deals with provisional attachment of property before conclusion of proceedings. For that Assistant Commissioner/Deputy Commissioner of customs has to take prior permission of commissioner. Such a provisional attachment is valid for a period of 6 months. With the permission of Chief Commission, it can be extended upto 2 years.

(B) Price of goods to indicate the amount of duty paid thereon (Section 28C)

Notwithstanding anything contained in this Act or any other law for the time being in force, every person who is liable to pay duty on any goods shall, at the time of clearance of the goods, prominently indicate in all the documents relating to assessment, sales invoice, and other like documents, the amount of such duty which will form part of the price at which such goods are to be sold.

(C) Presumption that incidence of duty has been passed on to the buyer (Section 28D)

Every person who has paid the duty on any goods under this Act shall, unless the contrary is proved by him, be deemed to have passed on the full incidence of such duty to the buyer of such goods.

It will be seen from provisions of Section 27, that a claim for refund of any duties paid must be made within one year or six months, as the case may be, except in

cases where any duty has been paid under protest. Payment of duty under “protest” signifies the involuntariness of the payment of tax. Hence, the statute itself lays down that the time bar will not apply.

The law dealing with refund of customs duty has undergone some changes including addition of some new sections like, Sections 28B, 28C and 28D. These amendments made by the Central Excises and Customs Laws (Amendment) Act, 1991 (w.e.f. 20.9.1991) are the direct result of Central Government’s attempt to prevent unjust enrichment of the assessee manufacturers/importers being accruing to them out of the refunds claims. The amending Act has made similar changes simultaneous in both Customs Act and the Central Excise Act, 1944.

The main features of these amendments are:

- (1) No refund of excise or customs duties are to be made to manufacturer/importer if duty incidence has already been passed on by him to the buyer.
- (2) Burden of proof that tax has not been passed on by him to buyer is to be on the claimant.
- (3) Refund is to be made only to the person who has ultimately borne the tax incidence.
- (4) Assessee is required to indicate, at the time of clearance of goods, in all assessment documents, the duty component of his sale price.
- (5) All amounts by way of Customs/Excise duties collected from the buyer in any manner are to be credited to Government forthwith.
- (6) A Consumer Welfare Fund is to be established to which any duty determined to be refundable will be credited, with a provision for its payment to an applicant only if he proves that the incidence of the duty has been passed on to him and that he has not passed on the incidence to some other person.
- (7) The aforesaid provisions shall have over-riding effect notwithstanding any judgement, decree, order or direction of the Tribunal or any Court or any other provision of the Customs Act or the Rules made there under or any other law.
- (8) Refund of—(a) export duty, (b) drawback and (c) duty on imports made by an individual for his personal use, however, are to be made to the importer only.
- (9) In the case of refund to buyer, period of limitation to run from the date of purchase of goods by him.
- (10) All refund applications in future to be in the prescribed form and the application should be accompanied by such documentary or other evidence (including the documents referred to in Section 28C) as the applicant may furnish to establish that the amount of duty in relation to which such refunds is claimed was collected from or paid by him and the incidence of such duty had not been passed by him to any other person.

The scheme framed by Sections 27, 28A, 28B, 28C and 28D, provides that ordinarily whenever an application for refund is granted, the refund goes to the

Consumer Welfare Fund and not to the applicant. This is because under Section 28D there is a presumption that every person who has paid duty on any goods has passed on the incidence of duty to the buyer of such goods. To rebut this presumption, the proviso to Section 27(2) requires the applicant to establish that he has not passed on the incidence of duty to the buyer of these goods, or has not sold these goods, but used them himself. Similarly, the buyer of such goods can get the refund if the buyer has not passed on the duty to anybody else. There are also provisions to ensure clear documentation indicating what is the price of such goods and how much is the duty on such goods and whether it is to be paid by the purchaser of such goods or not.

Hence, the entire scheme under the amended law is so designed that if the importer of goods, after clearing the goods on payment of duty, sells these goods to others and in the process passes on the incidence of duty to buyers, he will not be entitled for any refund. Only if he does not sell these goods that he will be entitled for the refund. Otherwise the refund will go to the buyer or to the persons to whom the buyer has further passed on the duty and if no rightful claimant is there, the refund amount will go to the Consumer Welfare Fund.

In *U.O.I. v. Solar pesticides (P) Ltd.* 2000 (116) ELT 401 (SC) held that the doctrine of unjust enrichment is applicable in respect of imported raw material captively consumed.

7.10 Recovery of duties not levied or short-levied or erroneously refunded (Section 28)

Where any duty has not been levied or has been short-levied or erroneously refunded, or any interest has not been paid or erroneously refunded, for—

- (1) any reason other than the reason of collusion or any willful mis-statement or suppression of facts then the proper officer shall within one year from the relevant date serve notice on the person chargeable with duty or interest requiring him to show cause why he should not pay the amount specified in the notice.

However the person chargeable with duty or interest may pay before the service of notice any amount of duty along with interest or interest on the basis of—

- (i) his own ascertainment of such duty or
- (ii) the duty ascertained by the proper officer

and inform the proper officer of such payment in writing, who, on receipt of such information shall not serve any notice in respect of duty or interest so paid. However proper officer can issue notice for the remaining amount.

- (2) the reason of—
 - (i) collusion; or
 - (ii) any willful mis-statement; or
 - (iii) suppression of facts,

by the importer or exporter or the agent or employee of the importer or exporter, the proper officer shall within 5 years from the relevant date, serve

notice on the person chargeable with duty or interest which has not been so levied or which has been so short-levied or short-paid or to whom the refund has erroneously been made, requiring him to show cause why he should not pay the amount specified in the notice.

However the person may pay the duty in full or in part, as may be accepted by him, and the interest payable thereon under Section 28AA and the penalty equal to twenty-five percent of the duty specified in the notice or the duty so accepted by that person, within thirty days of the receipt of notice and inform the proper officer about the payment in writing.

The proper officer then determine the amount of duty or interest and on determination, if proper officer is of the opinion—

- (i) that the duty with interest and penalty has been paid in full, then, the proceedings in respect of such person or other person to whom the notice is served, under Sub-section (1) or Sub-section (4) shall, without prejudice to the provision of Section 135, 135H and 140 be deemed to be conclusive as to the matters stated therein; or
- (ii) that the duty with interest and penalty paid falls short of the amount actually payable, then proper officer shall proceed to issue the notice in respect of the amount which falls short within a period of one year from the date of receipt of information about such payment.

The proper officer shall determine the amount within—

- (a) six months from the date of notice in respect of cases where duty has not been levied or has been short-levied or erroneously refunded, or any interest has been paid, part-paid or erroneously refunded, for any reason other than the reason of collusion or any willful mis-stated or suppression of facts.
- (b) within one year from the date of notice in respect of cases where reasons for non-levy, short levy or erroneous refund are collusion, any willful misstatement or suppression of facts.

“relevant date” means—

- (a) in a case where duty is not levied, or interest is not charged, the date on which the proper officer makes an order for the clearance of goods;
- (b) in a case where duty is provisionally assessed under Section 18, the date of adjustment of duty after the final assessment thereof;
- (c) in a case where duty or interest has been erroneously refunded, the date of such refund;
- (d) in any other case, the date of payment of duty or interest.

7.11 Power not to recover duties

Section 28A of the Customs Act, 1962 empowers the Central Government not to recover duties not levied or the difference in duty short-levied as a result of the practice that generally prevailed during the period the non-levy or short-levy

occurred. The rationale for this is that if all concerned—the assessee, the customs authorities and the consumers—had acted upon a certain basis, that basis should not be disturbed retrospectively and no demand should be made on that basis merely because subsequently a different assessment is regarded appropriate.

To give effect to this provision, the Central Government is required to issue a notification to this effect, in each such situation, giving the relief.

The section clearly aimed at providing equitable relief to assesseees who had in good faith paid less duty than was legally due. But in cases where duty was fully recovered as due under the law at the time of clearance, no refund of duty already paid was introduced in Section 28A, by the Customs and Excises Laws (Amendment) Act, which provided for refund even of the duty correctly levied at the time of clearance, provided the manufacturer proved that he had not passed it on to any other person. This new sub-section therefore empowered refunds being claimed and granted wherever eligible as a consequence of a notification issued under Section 28A(1).

With the growing controversy on refunds under central excises and customs and alleged unjust enrichment of assessment and consequent amendment in the laws on refunds under both excise and customs, Sub-section (2) of Section 28A has also been amended by the Central Excises and Customs Laws (Amendment) Act, 1991, whereby refunds under this section would be subject to the same provisions as refunds under Section 27, that is, the excess duty would be refunded to the tax bearer if he satisfies the prescribed conditions and otherwise credited to the Consumer Welfare Fund.

7.12 Interest on delayed payment of duty (Section 28AA)

As per the provisions of Section 28AA, the person who is liable to pay duty as per Section 28 shall, in addition to such duty, be liable to pay interest at a rate not below 10% and not exceeding 36% per annum, as may be fixed by Central Government may, by notification in the official gazette. The interest shall be paid for the period calculated from the first day of the month succeeding the month in which the duty ought to have been paid or from the date of erroneous refund, as the case may be, up to the date of payment of such duty. Clause 3 of Section 28AA provides that no interest is payable where the duty becomes payable consequent to the issue of an order, instruction or direction by the Board under Section 151A and such amount is voluntarily paid within forty-five days from the date of such order, instruction or direction and without reserving any right to appeal against said payment at any subsequent stage.

7.13 Recovery of duties in certain cases (Section 28AAA)

(1) Where an instrument issued to a person has been obtained by him by means of—

- (a) collusion; or
- (b) wilful misstatement; or
- (c) suppression of facts,

For the purposes of this Act or the Foreign Trade (Development and Regulation) Act, 1992, by such person or his agent or employee and such instrument is utilised

under the provisions of this Act or the rules made or notifications issued thereunder, by a person other than the person to whom the instrument was issued, the duty relating to such utilisation of instrument shall be deemed never to have been exempted or debited and such duty shall be recovered from the person to whom the said instrument was issued:

Provided that the action relating to recovery of duty under this section against the person to whom the instrument was issued shall be without prejudice to an action against the importer under section 28.

Explanation 1.—For the purposes of this sub-section, "instrument" means any scrip or authorisation or licence or certificate or such other document, by whatever name called, issued under the Foreign Trade (Development and Regulation) Act, 1992, with respect to a reward or incentive scheme or duty exemption scheme or duty remission scheme or such other scheme bestowing financial or fiscal benefits, which may be utilised under the provisions of this Act or the rules made or notifications issued thereunder.

Explanation 2.—The provisions of this sub-section shall apply to any utilisation of instrument so obtained by the person referred to in this subsection on or after the date on which the Finance Bill, 2012 receives the assent of the President, whether or not such instrument is issued to him prior to the date of the assent.

(2) Where the duty becomes recoverable in accordance with the provisions of sub-section (1), the person from whom such duty is to be recovered, shall, in addition to such duty, be liable to pay interest at the rate fixed by the Central Government under section 28 AA and the amount of such interest shall be calculated for the period beginning from the date of utilisation of the instrument till the date of recovery of such duty.

(3) For the purposes of recovery under sub-section (2), the proper officer shall serve notice on the person to whom the instrument was issued requiring him to show cause, within a period of thirty days from the date of receipt of the notice, as to why the amount specified in the notice (excluding the interest) should not be recovered from him, and after giving that person an opportunity of being heard, and after considering the representation, if any, made by such person, determine the amount of duty or interest or both to be recovered from such person, not being in excess of the amount specified in the notice, and pass order to recover the amount of duty or interest or both and the person to whom the instrument was issued shall repay the amount so specified in the notice within a period of thirty days from the date of receipt of the said order, along with the interest due on such amount, whether or not the amount of interest is specified separately.

(4) Where an order determining the duty has been passed under section 28, no order to recover that duty shall be passed under this section. (5) Where the person referred to in sub-section (3) fails to repay the amount within the period of thirty days specified therein, it shall be recovered in the manner laid down in sub-section (1) of section 142.

7.14 Assessment of duty (Section 17)

Section 17 of the Customs Act, prescribes the method for assessment of duty. As per Sub-section (1) any importer entering any imported goods under Section 46

or an exporter entering any export goods under Section 50, shall self assess the duty, if any leviable on such goods. However nothing shall apply to stores under Section 85.

The proper officer may verify the self assessment of the goods and for this purpose examine or test any imported goods or exported goods.

The proper officer may require the importer, exporter or any other person to produce any contract, broker's note, insurance policy, catalogue or other documents, whereby the duty leviable on the imported goods or export goods can be ascertained.

Where it is found on such verification, examination or testing of the goods, or otherwise that the self assessment is not done correctly, then the proper officer may, without prejudice to any other action which may be taken under this act, re-assess the duty leviable on such goods.

Where any re-assessment done under Sub-section (4) is contrary to the self-assessment done by the importer. The proper officer shall pass a speaking order on the re-assessment within fifteen days from the date of re-assessment of the bill of entry or the shipping bill.

Where re-assessment has not been done or a speaking order has not been passed on re-assessment, the proper officer may audit the assessment of duty of the imported goods or export goods at his office or at the premises of the importer or exporter, as may be expedient, in such manner as may be prescribed.

Explanation: For the removal of doubts, it is hereby declared that in cases where an importer has entered any imported goods under Section 46 or an exporter has entered any export goods under Section 50 before the date of Finance Bill, 2011 receives the assent of the President, such imported goods or export goods shall continue to be governed by the provisions of Section 17 as it stood immediately before the date on which assent is received.

7.15 Provisional Assessment of Duty (Section 18)

The Act also provides for a provisional assessment of duty under certain circumstances, as for instance, where the proper officer deems it necessary to subject any imported goods or export goods to any chemical or other tests for the purpose of assessment of duty thereon or where the importer or exporter has produced all the necessary documents and furnished full information for the assessment of duty but the proper officer deems it necessary to make further enquiry for assessing the same. Section 18 which deals with ***procedure for provisional assessment read as follows:***

(1) Notwithstanding anything contained in this act but without prejudice to the provisions contained in Section 46—

- (a) where the importer or exporter is unable to make self-assessment under Sub-section (1) of Section 17 and makes a request in writing to the proper officer for assessment; or
- (b) where the proper officer deems it necessary to subject any imported goods or export goods to any chemical or other test; or

- (c) where the importer or exporter has produced all the necessary documents and furnished full information but the proper officer deems it necessary to make further enquiry; or
- (d) where necessary documents have not been produced or information has not been furnished and the proper officer deems it necessary to make further enquiry.

The proper officer may direct that the duty leviable on such goods be assessed provisionally if the importer or the exporter, as the case may be furnishes such security as the proper officer deems fit for the payment of the deficiency, if any, between the duty as may be finally assessed and the duty provisionally assessed.

(2) When the duty leviable on such goods is assessed finally or reassessed by the proper officer, then —

- (a) in the case of goods cleared for home consumption or exportation, the amount paid shall be adjusted against the duty finally assessed or reassessed and if the amount so paid falls short of, or is in excess of the duty finally assessed or reassessed, the importer or the exporter of the goods shall pay the deficiency or be entitled to a refund, as the case may be;
- (b) in the case of warehoused goods, the proper officer may, where duty finally assessed or reassessed is in excess of the duty provisionally assessed, require the importer to execute a bond, binding himself in a sum equal to twice the amount of the excess duty.

(3) The importer or exporter shall be liable to pay interest, on any amount payable to the Central Government, consequent to the final assessment order or reassessment order under sub-section (2), at the rate fixed by the Central Government under Section 28AB from the first day of the month in which the duty is provisionally assessed till the date of payment thereof.

(4) Subject to sub-section (5), if any refundable amount referred to in clause (a) of sub-section (2) is not refunded under that sub-section within three months from the date of assessment of duty finally or reassessment of duty, there shall be paid in interest on such unrefunded amount at such rate fixed by the Central Government under Section 27A till the date of refund of such amount.

(5) Amount of duty refundable under Sub-section (2) and the interest under Sub-section (4), if any, shall, instead of being credited to the Fund, be paid to the importer or the exporter, as the case may be, if such amount is relatable to—

- (a) the duty and interest, if any, paid on such duty paid by the importer, or the exporter, as the case may be, if he had not passed on the incidence of such duty and interest, if any, paid on such duty to any other person;
- (b) the duty and interest, if any, paid on such duty on imports made by an individual for his personal use;
- (c) the duty and interest, if any, paid on such duty borne by the buyer, if he had not passed on the incidence of such duty and interest, if any, paid on such duty to any other person;

- (d) the export duty as specified in Section 26;
- (e) drawback of duty payable under Sections 74 and 75.

The provisional assessment of duty is possible only when the provisions of Section 18 of the Customs Act, 1962 are satisfied but in the event of the conditions mentioned there in not being satisfied by the petitioner, it cannot be said that the assessment was made provisionally at the time of the clearance of the goods for home consumption.

The Central Government has under notification No. 181/63-Cus. dated 13th July, 1963 framed certain regulations governing provisional assessments. These regulations are known as Customs (Provisional Duty Assessment) Regulations, 1963.

7.16 Advance Ruling

The Finance Act, 1999 has introduced Chapter VB under the Customs Act, 1962 consisting of Sections 28E to 28M. This Chapter has been incorporated with a view to provide binding rulings on important issues, so as to enable the intending assesseees to have a clear cut indication of their duty liability in advance. The Chapter provides for appointment of 'Authority for Advance Rulings' which would pronounce rulings regarding rate and quantum of duty payable in advance for the benefit of joint ventures with NRIs.

This Authority has been appointed somewhat on similar lines of the Advance Ruling Authority on the Direct Taxes. The system of Advance Ruling has been existing in the USA and certain European countries for many years. This concept was considered in India by Wanchoo Committee far back in 1971. However, it was only after the 1991 reforms consequent upon our policies of liberalisation and globalisation which brought in India considerable foreign investments that a scheme of Advance Ruling finally found its place on the statute book by Finance Act, 1993 and Chapter XIX-B was inserted in the Income-tax Act, 1961, w.e.f. 1.6.1993. Now, the provisions regarding 'Advance Rulings' have been introduced for the first time by the Finance Act, 1999 as regards Customs and Central Excise both. Separate Chapters, namely, Chapter V-B (Sections 28E to 28M) and Chapter III-A (Sections 23A to 23H) have been inducted in the Customs Act, 1962 and Central Excise Act, 1944 respectively. The provisions of Advance Rulings are almost identical in both Customs and Central Excise. The scheme of Advance Rulings is along the same lines as in the scheme presently contained in the Income-tax Act, 1961.

(A) Salient Features of the Scheme

- (a) Authority for Advance Ruling is to be constituted under Section 28F of the Customs Act, 1962 and would exercise jurisdiction on all applications under the Central Excise Act, 1944 also by virtue of Section 23A(e) of the Central Excise Act, 1944. (The Finance Act, 2009 has modified Section 28F to provide that the Central Government may by notification authorize the Authority for Advance Rulings constituted under Section 245-O of the Income Tax Act to act as an Authority for the purposes of customs, central excise and service tax subject to certain some modification regarding the constitution of the Authority.)

- (b) This Authority can determine a question of law or fact specified in the application, questions relating to classification of goods, exemption notifications and valuation of goods under both the Acts.
- (c) The Advance Ruling can only relate to the liability to pay customs duty (or excise duty) on an activity proposed to be undertaken which is to be carried out in future.
- (d) The proceedings are commenced at the instance of applicants who are necessarily persons Setting up joint ventures, some or all of whom are NRIs and the Commissioner of Customs/Central Excise would be a party to the proceedings within whose jurisdiction the activity of import or export/ manufacture is sought to be carried on.
- (e) The Authority for Advance Rulings would not allow the application if the question raised is pending, in the applicant's case, before Customs/Central Excise Officer, the Appellate Tribunal or any court or when the same issue has already been decided by the Appellate Tribunal or a Court.
- (f) The ruling issued under the scheme would be binding on the applicant and the concerned Commissioner of Customs/Central Excise as the case may be, including their sub-ordinate officers and staff. If there is any change in law or in the facts, the ruling issued would not be binding.
- (g) An application for 'Advance Ruling' can be made by the applicant in quadruplicate alongwith a fee of ₹ 2,500/-. However, withdrawal of application can be made within 30 days from its date.
- (h) The authority for advance ruling is required to pronounce its advance ruling in writing within 90 days from the date of its application.
- (i) A ruling which is obtained by fraud or suppression of facts is declared void *ab-initio*.
- (j) The office of the authority would be located in Delhi and would consist of three members, i.e., the Chairperson who would be a retired judge of the Supreme Court, an officer of Indian Customs/Central Excise service qualified to be a member of Central Board of Excise and Customs and an officer of the Indian Legal Service qualified to be an Additional Secretary to the Government of India.
- (k) The authority so appointed would have the powers of a civil court under the Civil Procedure Code, 1908 like powers of discovery, inspection, enforcing attendance of any person, examining him on oath and of issuing commissions and compelling production of books of account and other records etc. The proceedings before the authority are deemed as, "judicial proceedings".
- (l) The authority would have the power to regulate its own procedure in all matters arising out of the exercise of its powers under the Customs and Excise Statutes.

Similar provisions for appointment of authority for Advance Rulings have also been made under Central Excise Act, 1944 by insertion of a new Chapter III-A

(Sections 23A to 23H) respectively except the Section 28F of the Customs Act, 1962 providing for authority for advance ruling, rest of the provisions are on similar lines.

Joint venture in India means a venture in which at least one of the participants, partners, or equity holders shall be a non resident having substantial interest in the joint venture and exercising joint control over it.

7.17 Clearance of Imported or Exported Goods including Baggage

As per Section 12, of the Customs Act, 1962, customs duties are levied on goods imported into or exported from India at such rates as may be specified under the Customs Tariff Act, 1975 or under any other law for the time being in force. While the rates of duties are fixed under the Customs Tariff Act, the levy of duties (and collection thereof) is regulated by the Customs Act, 1962. India has a long coastal line with ports, (landing and loading places) spread over and also a long (land) border with the neighbouring countries. For effective discharge of the functions of the Customs Department, viz., (i) to collect Revenue on Import & Export, (ii) to prevent smuggling, and (iii) to enforce prohibitions and restrictions in regard to imports and exports imposed under the Customs Act, 1962 (Section 11 of the Customs Act, 1962) and other allied enactments, such as The Imports and Exports (Control) Act, 1947, The Foreign Exchange Management Act, 1999 etc., to refer to a few, it is imperative that the Import of goods and Export of goods are regulated to take place through certain specified/ approved/authorised ports/places etc. Therefore, for the purposes of importing and exporting goods the Board (Vide Section 7 of the Customs Act, 1962) notifies:

- (a) the ports (and the Airports) for unloading of Imported goods and loading of Export goods;
- (aa) the places which alone shall be inland container depots for the unloading of imported goods and loading of export goods or any class of such goods.
- (b) the places for clearance of goods imported or to be exported;
- (c) the routes by which alone goods may pass by land or inland water in to or out of India; and
- (d) the ports which alone shall be 'Coastal ports' under the Customs Act.

Under Section 8, of the Customs Act, 1962, Commissioners of Customs, have been invested with the power to specify the places within a Customs port or Customs Airport or Coastal port for unloading and/or loading of goods. Therefore, any Import or export taking place at/through/from places other than those notified ports/places is held to be unauthorised - rendering the goods attempted to be landed, loaded, including the conveyance (i.e. the vessel, the Aircraft or the Vehicle) liable for confiscation (under Sections 111, 113 and 115 of Customs Act respectively) and the persons concerned, including the abettor, in such landing, loading are liable to penalty (under Sections 112, 114 of Customs Act, 1962) without prejudice for prosecution (under the Customs Act, 1962) before a court of law.

7.17.1 Clearance of Import Cargo

The organisations which play vital roles in the clearance of Import cargo are:

- (i) The Steamer Agents/Airline Companies as the case may be (who are "appointed by the person incharge of a conveyance and who represent to

any officer of Customs as an agent, (Section 148, Customs Act) who transport the goods to India, (carriers).

- (ii) The Port Trust Authorities or International Airport Authorities of India (IAAI) (in case of air consignments) who are approved by the Commissioner of Customs as Custodians of Imported Cargo, (Section 45 of the Customs Act, 1962) who act as bailees and are responsible for the receipt, storage, custody and delivery of the goods, after the customs formalities are complied with by the Importers.
- (iii) The Custom House Agents who are licenced by the Commissioner of Customs (Section 45 of the Customs Act, 1962) to carry on business as an agent relating to the entry or departure of a conveyance or the Import or the Export of goods at any customs station. The agents are licensed in accordance with the Custom House Agents (Licensing) Regulations which inter alia provide for:
 - (a) the validity of any such licence, the fees payable therefore;
 - (b) the qualification of persons who may apply for a licence;
 - (c) the qualifications of persons to be employed by a licensee to assist him in his work as an agent;
 - (d) the restrictions and conditions subject to which a licence may be granted.
- (iv) The Custom Houses comprising particularly Customs Officers of the Appraising Department, viz., the Deputy Commissioner, Appraisers, Examiners and supporting ministerial staff as well as various other units in the Customs House.

7.17.2 Imported goods — Provisions in the Customs Act, 1962

By definition under Section 2(23) of the Customs Act, 1962, 'Import' with its grammatical variations and cognate expressions, means bringing into India from a place outside India.

'Import goods' in terms of Section 2(25) of the Customs Act, 1962, means "any goods brought into India from a place outside India but does not include goods which have been cleared for home consumption".

'Importer' has been defined under Section 2(26), as including any owner or any person holding himself out to be the importer in relation to any goods at any time between their importation and the time they are cleared for home consumption.

Sections 45 to 49 of the Customs Act, 1962 cover clearance, of "imported goods". Generally all imported goods are to be 'unloaded' in 'appointed Customs Ports, Airports' (appointed by Central Government by notification in the official Gazette - (Section 7 of Customs Act, 1962) and in 'proper place "approved" as landing places' - "Customs area" by the Commissioner of Customs (of the respective jurisdiction) specifying the limits (Section 8 of the Customs Act, 1962).

Further, "the person incharge of a vessel or an Aircraft entering India from any place outside India shall not cause or permit the vessel or Aircraft to call or land at any time while it is carrying cargo at any place other than a Customs port or Customs Airport as the case may be". (Section 29 of the Customs Act, 1962).

All Imported goods unloaded in a Customs area, are required to remain in the custody of the person approved by the Commissioner of Customs, until they are cleared for home consumption, or are warehoused or transhipped. In major ports, the approved custodians are the Port Trust or Port Commissioners and in International Airports, the IAAI authorities. These approved bailees have control over imported goods. Under the statute (Section 45 of the Customs Act, 1962), the above 'Approved custodians' shall keep a record of such goods and send a copy thereof to the "proper officer" of Customs and shall not permit such goods to be removed from the Customs area or otherwise dealt with, except under and in accordance with the permission in writing of the 'proper officer' of Customs.

Under the Imported Package (Opening) Regulations, 1963, no person shall, except with the permission of the proper officer, open any packages of goods imported into India and lying in a Customs area.

In Minor Ports and in Land Customs Stations, Imported goods brought by vessels, vehicles (conveyances) and unloaded are in the custody of the Customs Officers.

7.17.3 Procedure for clearance of the goods

Goods imported can be unloaded from the Steamers, particularly, in the 'Customs Station' only after an order is given by the proper officer of Customs, granting "Entry Inwards". Granting "Entry Inwards" is contingent upon certain formalities being complied with, by the person 'In charge' of a conveyance and/or his 'agent'.

Import Manifest

The Carrier-in charge of a vessel carrying imported goods furnishes a record of the goods carried by him and it is called a Import Manifest. Under Section 30(1) of the Customs Act, the Import Manifest is required to be filed before the arrival of the vessel or aircraft. In the case of a vehicle, it is within 12 hours after arrival. The forms of the Import Manifest are prescribed in the Import Manifest (Vessels) Regulations, 1971 and Import Manifest (Air Craft) Regulations, 1976, which have been made under Section 157 of the Customs Act, 1962.

In practice the Steamer Agents, acting on behalf of the Master of the Ship, file the Import Manifest in the Import Department of the Customs House before the actual arrival of the ship at the port. This is done to enable the importers to file their documents and complete as much of the Customs formalities as possible, before the arrival of the ship so that, there is no delay in the clearance of the cargo when they are landed. Proviso (a) to Section 30(1) of the Customs Act provides for presentation of Import Manifest even before the arrival of the Steamer.

The Import Manifest is required to be delivered in duplicate in the Import Department with full particulars in respect of the following:

- (i) General declaration (giving information mainly about the vessel, its Master, number of crew, passengers);
- (ii) Cargo declaration;
- (iii) Vessel's Store List; and
- (iv) List of private property in the possession of Master, Officers and Crew.

Separate particulars are required to be furnished in the cargo declaration in respect of:

- (a) Cargo to be landed;
- (b) Same Bottom Cargo - 'Cargo in transit';
- (c) Cargo for transshipment; and
- (d) Unaccompanied Baggage.

The information required to be given with regard to the Cargo to be landed at the Port, includes identifying particulars (marks and numbers) of the packages etc. The Serial Number in the Manifest for a particular consignment is known as the "Line number" of the Manifest. The documents filed for clearance bear this line number for purposes of co-relating the clearance documents with the entry in the Manifest.

Steamer Agents acting on behalf of the master of the vessel are accountable to the department for all the goods mentioned in the Manifest as for import into India (Section 116 of the Customs Act, 1962). Steamer Agents in this regard file undertaking(s) and also a guarantee to pay any penalty that may be imposed under Section 116, if they do not account for, to the satisfaction of the Assistant Commissioner of Customs, or for their failure to unload any goods or for any deficiency in the unloaded goods.

In regard to Air Consignments, the 'Import Cargo Manifest' is presented in Triplicate or Quadruplicate by the persons concerned immediately on landing of the Aircraft and the cargo as detailed in the Manifest as intended for landing are checked by the Customs Officers (Import Freight Officers of the Preventive formation) and then made over for custody to the International Airports Authority of India (IAAI).

The cargo manifest is then sent to the Customs Appraising Formation (Air Cargo Complex) by the Import Freight Officer.

Assignment of Import Rotation Number

On receipt of the Import Manifest in the Import Department of the Customs House and at the Air Cargo Complex as the case may be, it is checked and an import rotation number assigned to the vessel/Aircraft for the particular voyage. The rotation number is the running serial number for each calendar year in respect of the Manifest filed.

Entry of Goods on Importation

Under Section 46(1) of the Customs Act, an Importer of any goods, other than goods intended for Transshipment is required to file electronically a "Bill of Entry for home consumption" or "for warehousing". The Bill of Entry *inter alia*, has columns for indicating description of goods, value, quantity, marks and numbers, country of origin etc. Bill of Entry is required to be presented electronically, however, the commissioner of customs may, in cases where it is not feasible to make entry by presenting electronically allow an entry to be presented in any other manner. If the Bill of Entry at the time of presentation is not reasonably complete in all material particulars, the same is liable to be returned by the Customs Department for necessary completion of all the details and resubmission.

Kinds of Bills of Entry

There are three kinds of Bills of Entry viz., (i) Bill of Entry for Home-consumption

(White Colour) (ii) Warehousing (into-Bond) Bill of Entry (Yellow Colour) (iii) Bill of Entry for Clearance 'Ex-Bond' (Green Colour).

Forms of the Bill of Entry

The home-consumption Bill of Entry which is printed on white paper is referred to as "white Bill of Entry", the "into Bond" or "Warehousing Bill of Entry" is printed on yellow paper and "ex-bond" is printed on green paper. Each Bill of Entry has to be filed in quadruplicate. The columns in original are printed in black, in blue in duplicate and in violet in triplicate and in green in quadruplicate.

The original Bill of Entry is retained in the Customs House after payment of duty and is never handed over back to the Importer or his agent, once duty is paid. The duplicate and triplicate and quadruplicate are handed over to the party after payment of the duty. The triplicate copy of the Bill of Entry serves the purpose of a receipt for having paid duty and the quadruplicate is produced to the bankers for allowing remittance towards payment to the foreign suppliers of the goods. The duplicate, is taken to the Docks/examination area of Air Cargo Complex (in respect of air consignments) where imported goods are stored. Examination of the goods is done by the Customs Examiners and Appraisers at the Docks/Air-Cargo before they permit delivery of the goods.

An Importer, while presenting a Bill of Entry, is required to make a declaration as to the truth of the contents of the Bill of Entry and in support of such declaration, he should produce to the proper officer of customs, the invoice etc. relating to the imported goods, it is, however, possible that in certain cases an importer may not be in a position to give such a declaration. In such an eventuality, if he declares, that he is unable, for want of full information, to furnish the relevant particulars of the goods as required under the law, the Assistant Commissioner may permit him, before filing a Bill of Entry, to examine the goods in the presence of an officer of Customs. This provision gives an opportunity to the importer to make his declaration in the Bill of Entry, after seeing the goods imported by him. The Customs Officer is however to verify, as to whether declaration, made by importer after having seen the goods is correct or not.

The following basic documents are to be filed along with the Bill of Entry:

1. Invoice.
2. Indent and acceptance correspondence pertaining to the Imported goods.
3. Bill of Lading in respect of sea-consignments/Airway Bill in respect of Air Consignments.
4. Letter of credit or Bill of exchange.
5. Insurance policy or Insurance certificate.
6. Import licence (Customs purpose copy).
7. Small Scale Industries Certificate in respect of Imports sought to be covered under Open General Licence (OGL) and Imports subjected to Actual Users (AU) conditions.
8. Catalogue, drawing, write up, analysis certificate as the case may be, in respect of the goods sought to be cleared.
9. Any other connected/relevant document.

The Bill of Entry is first presented to the Import Department of the major Custom House or in Air Cargo Complex as the case may be. The Bill of Entry is numbered, dated and then “noted” in the relative import manifest of the particular vessel, provided all the particulars as declared, in the Bill of Entry agree with those shown against the relative “entry” in the Import Manifest. If there are discrepancies, the Bill of Entry is returned for proper clarification and re-submission. The date on which the Bill of Entry is “presented” is important in determining the rate of duty, tariff value and rate of exchange applicable to the goods covered by the Bill of Entry. In the case of bills of entry filed/presented under the “prior entry” system (i.e. cases wherein bills of entry are filed by the importers or Custom House Agents before the arrival of the vessel) the rate of duty and tariff value will be those prevailing on the date of “entry inwards” of the vessel and not those prevailing on the date of filing of the Bill of Entry.

When a Bill of Entry is “presented” in the Import Department or in Air Cargo Complex as the case may be, it is checked to see as to whether all relevant columns in the Bill of Entry have been filled in and that all corrections and amendments are attested by the importer or his Agent. Declarations required to be made on the Bill of Entry duly signed by all concerned are also checked.

The Bill of Entry is thereafter returned to the importer or his Agent, who presents it to the concerned ‘Groups’, in the Appraising Department. The Appraising Department in the Custom houses are divided into groups by which arrangement the goods/commodities as contained in the Tariff are so distributed between the groups, that the work load is equitable among the various Groups. Each Group is under the charge of an Assistant Commissioner with sufficient number of Appraisers and requisite ministerial staff.

The Bills of Entry presented in the Groups by the importers or their agents every day, are received by means of a date stamp on each and distributed among the concerned Appraisers.

The Appraiser —

- (i) checks the correctness of the value declared on the Bill of Entry, with reference to the supporting documents;
- (ii) classifies the goods under the First Schedule to the Customs Tariff Act, 1985 (Import Tariff), as well as the Central Excise Tariff and apply the correct rates of basic, auxiliary and countervailing duties;
- (iii) verifies that the goods have not been imported in contravention of “any prohibitions or restrictions” either under the Customs Act or under any other allied Acts for which the Customs Department performs the agency functions; and
- (iv) initiates appropriate action as deemed necessary and as warranted, for any violation under the Customs Act or any other law.

While verifying the importer’s declaration regarding the value and for classification of goods, the following documents amongst others, that are filed along with the Bill of Entry, are scrutinised, by the Appraisers:

- (i) Invoice, packing list;

- (ii) Brokers' note or indenting agent's quotation, if any;
- (iii) Catalogue, drawing or other literature;
- (iv) Contract with suppliers or indent and acceptance;
- (v) Import Licence.

If the invoice value is "net", the "gross" value should also be indicated. If the importer has "special relationship" such as an "agent" or "collaborator" of the foreign suppliers, that facts should be clearly declared in the relevant declaration required to be filled in the Bill of Entry. The Appraiser may call for documents like catalogues [also parts catalogue] in cases where (spare) parts are imported, technical write-up and any other relevant document which he, as the Assessing Officer, may require for the purpose of assessing the Bill of Entry. Section 17(3) of the Customs Act, 1962 authorises the importer exporter or any other person to call for these documents or information, for verification and for scrutiny in the course of assessment.

Recently, computerisation has been introduced in some Customs Houses. The procedures are still at the experimental stage. However, the Forms of Bill of Entry have been re-issued (w.e.f. 1.7.88). (Students may see the computerised proforma of various Bill of Entry Forms in the latest customs manual).

Clearance of goods for home consumption

An order permitting clearance of goods for home consumption is made by the proper officer under Section 47(1) of this Act. According to Sub-section (1) where the proper officer is satisfied that any goods entered for home consumption are not prohibited goods and the importer has paid the import duty, if any, assessed thereon and any charges payable under this Act in respect of the same, the proper officer may make an order permitting clearance of the goods for home consumption.

Chargeability of interest under Section 47(2)

This refers to chargeability of interest under Section 47(2) of the Customs Act, 1962 where the duty initially assessed on a Bill of Entry was subsequently re-assessed to Nil rate of duty. The Board has observed that assessment includes re-assessment of duty. Hence, where goods are re-assessed to duty, the said duty is the material duty as per Sub-section (1) of Section 47 of the Customs Act, 1962. A close reading of the provisions of Sub-section (1) of Section 47 shows that the duty referred to in this sub-section is the one assessed proximate to the passing of the order permitting clearance of the goods. Further more, as per Sub-section (2) of Section 47 the interest liability arises if the duty assessed as per Sub-section (1) is not paid. This duty in the instant case is the re-assessed duty. Therefore, a harmonious reading of the provision of Sub-sections (1) and (2) of Section 47 would lead to the conclusion that the relevant duty for purpose of interest levy is the duty assessed immediately prior to the stage of the proper officer permitting clearance of the goods.

These observations were made in a case where a particular importer filed a Bill of Entry for home consumption of the imported item through a major Custom House. The assessment was finalised and the Bill of Entry returned to the importer for payment of duty. The importer did not, however, clear the goods after duty payment.

Subsequently, the importer sought re-assessment of his goods on the strength of Advance licences obtained by him for clearance under DEEC Scheme. The Bill of Entry was accordingly re-assessed at Nil rate of duty. A doubt, however, arose regarding relevant duty for purpose of leviability of interest under Section 47(2) of the Customs Act, 1962.

In view of the aforesaid decision of the Board it is informed that interest under Section 47(2) of the Customs Act, 1962 should be levied w.r.t. duty assessed (or re-assessed) proximate to the proper officer permitting clearance of the goods on payment of the said assessed (or re-assessed) duty. [Based on Commissioner of Customs, New Delhi, Public Notice No. 43/97, dated 9.5.1997].

Crucial date for calculating interest under Section 47 of the Customs Act, 1962

As per the provisions of Section 47(2) of the Customs Act, 1962, interest is payable on such goods in respect of which Bill of Entry for home consumption has been assessed and returned to the importer but the duty leviable thereon has not been paid within five days excluding holidays of such return. Certain instances have been brought to the notice of the Board where the Bill of Entry had been filed by the importer but due to some reason or the other the vessels arrived very late or could not get a berth vessel was much after the return of the assessed Bill of Entry. Thus, interest liability arose in respect of such goods even when these goods have not even been landed on the Indian shores. It has been represented that the situation is anomalous and some what unjust towards the importer.

The matter has been accordingly examined by the Board. The Board has observed that in case of prior Bill of Entry, the effective date for determining the rate of duty was the date of entry inward of the vessel, in case where the Bill of Entry were assessed and returned prior to the entry of the vessel, the Bill of Entry were required to be returned to the custom house for completion of assessment formalities before being returned to the importer for payment of duty. Hence, in order to resolve the anomalous situation it has been decided that the relevant date i.e. the date of return of the assessed Bill, of Entry should be the date of completion of assessment of the Bill of Entry on its submission to the Customs House after entry inward is granted to the vessel. The period of five days excluding holidays for purpose of interest levy should be calculated from this date of finalisation of assessment. [Based on Commissioner of Customs, New Delhi, Public Notice No. 44/97, dated 9.5.1997].

Procedure in regard to goods not cleared

Section 48 of the Customs Act, 1962 provides for the sale of the goods brought into India by the proper officer of customs in case the goods are not cleared for home consumption or warehoused or transhipped within "thirty days" from the date of the unloading at a customs station. The uncleared goods (Bill of Entry) Regulations, 1972 (framed in exercise of powers conferred by Section 157 of the Customs Act, 1962) provides the procedure to be followed for this purpose. According to Regulation 2 of these Regulations, the person having the custody of goods that are not cleared for home consumption within the period specified in Section 48 of the Customs Act, 1962 (52 of 1962) (hereinafter referred to as the said Act) shall prepare a Bill of Entry in the form appended (Form 60) to these Regulations, of such goods to be sold in auction.

Regulation 3 provides that the Bill of Entry prepared under Regulation 2 shall be deemed to be the Bill of Entry under Sub-section (2) of Section 46 of the said Act and presented to the proper officer.

Provided that the said Bill of Entry shall not be deemed to be the Bill of Entry in respect of goods which are not actually sold in the auction held for the sale of goods specified in that Bill of Entry, and actually delivered to the buyer.

Examination of goods before order of Clearance is given

An Assistant Commissioner is in charge of the Customs Examination unit in the Docks/Air Cargo Complex and is assisted by several Appraisers. The work of physical examination and quantitative verification of imported goods is carried out by the Examiners, whereas appraisal of value and classification (wherever needed) are done by the Appraisers. Selected packages only are normally and under bona fide circumstances examined. Cargo is stocked in the 'transit shed' according to marks and numbers, relating to a particular consignee and the packages selected for examination are brought to the Customs Examination Yard, set apart, in each transit shed. Examination includes weighing and measurement and the Examination Report is written immediately after the examination is conducted.

Certain types of imported goods require special treatment; for example, plants coming into the country will have to be fumigated by the Plant Quarantine Department for purposes of the requirements under the Destructive Insects and Pests Act. Similarly, hazardous cargo imported from abroad will have to be examined only in the hazardous cargo shed provided by the Port Trust/handling agencies.

The Bills of Entry are presented to the Appraiser in charge of the shed, who examines the goods at the Customs Examination Yard with the assistance of the Examiner, verifies as to whether everything is in order in relation to the imported goods as covered by the Bill of Entry and various declarations made therein; that the duty due has actually been paid and then gives an order that the goods are "out of Customs Charge". He also verifies wherever necessary that fines or penalties levied, if any, as a result of adjudication have also been recovered and suitable endorsements to that effect have been made by the department on the Bill of Entry.

If at the time of examination, the shed Appraiser finds that the goods actually imported are not in conformity with the declaration made by the importer and as accepted by the assessing Appraiser, on the basis of documents filed, he does not sign the "out of charge" order. Instead, he returns the Bill of Entry to the concerned Group with suitable remarks on classification and assessment or for reconciliation of the discrepancy pointed out by him.

As mentioned earlier, in such of those cases, where the Appraiser in the Assessing Group is not in a position to make an assessment on the basis of the documents filed, such as, invoices, catalogues or other literature and he feels that before the assessment, the goods should be examined or tested, he gives an order for such examination by the Customs Staff in the sheds/docks and the assessment is termed as "First Appraisal System", i.e. the system by which the goods are examined first and subsequently only assessed to duty. In such cases, the assessing appraiser endorses an order on the reverse of the original copy of the Bill of Entry to open, as many packages as are necessary and required for proper valuation and/or

classification of the goods. Such verification is done by the Examiners and Appraisers in the Docks. If the assessing Appraiser in spite of the examination report furnished is still not satisfied with the details made available to him by the Officer in the Docks, he himself may visit Docks to see the goods for himself, before completing the valuation and assessment on the Bill of Entry. In this first appraisal system after the examination of the goods and assessment by the Appraiser and payment of duty, the Office Superintendent in the Accounts Department signs the 'out of Customs Charge' order for delivery of the goods to the Importer.

Forwarding of Duplicate Bill of Entry by Port Trust

After the goods delivered to the importers by the Port Trust, the latter collect the duplicate bills of entry and send them over to the Internal Audit Department of the Customs House where the original copies of bills of entry already sent after collection of duty are matched with the duplicate copies for purposes of audit. After audit, they find place in the Import Manifest of the relative steamer to form the ship's file.

Clearance of Goods Imported by Post

Apart from imports by sea and air, goods are also imported through the medium of the post. The procedure for clearance of goods imported by post differs in various aspects from that applicable for imports by sea and air. The differences are essentially in the manner of entry, custody and delivery of the goods and also in the mode of payment of duty. Apart from the restrictions imposed under the Customs Act in respect of such imports, certain restrictions are also imposed under the Indian Post Office Act, 1898.

Clearance of goods imported by post is governed by Sections 82, 83 and 84 of the Customs Act, 1962.

Section 82 lays down that, in the case of goods imported by post any label or declaration accompanying the goods showing the contents, description, quantity and value, should be treated as "an entry for import" for the purpose of the Act.

Section 83(1) of the Customs Act, 1962 defines the crucial date for the determination of rate of duty and tariff value applicable to such goods. The crucial date is the date on which the postal authorities present to the proper officer of Customs in the Postal Appraising Department a list (called Way Bill) containing particulars of the parcels or packets for the purpose of assessment to duty. However, if the goods are imported by a vessel (Surface mail) and the list is presented before the arrival of the vessel, the crucial date is the date of arrival of the vessel.

Functions of the Foreign Post Office

The Foreign Post Office receives inward foreign mails and forwards them to the local post offices for delivery to the addressees. Customs Department is concerned only with levy of Customs duty on the goods imported and also with the prevention of entry of unauthorised or otherwise "prohibited or restricted" goods. In the Foreign Post Office, both the Customs and Postal departments function side by side and work in close liaison with each other. But custody of the foreign parcels remains with the post office throughout the journey. The post office is responsible for the contents and handling of the parcels.

Parcels coming to India are accompanied by Customs declarations. The Post Office receives an advice of despatch notes, together with Customs declarations in duplicate from the authorities of the foreign country from which they are imported. Foreign Post Office also prepares local parcel bills or Way bills showing particulars such as office of posting, original foreign number, name of the addressee, full address and local serial number etc. The Way Bills are forwarded by them to the Postal Appraising Department along with the above documents.

Sheet Assessment

Way Bills are presented by the Postal Department to the Postal Appraising Department for "Sheet Assessment" (also known as direct assessment) by Appraisers or Examiners. Such assessment includes assessment and pre-audit of all assessable parcels, designating parcels required for first appraisal, detaining parcels requiring documents, and preparation and despatch of notices of call.

Examination

Each Assessing Officer in the Postal Appraising Department is assigned a "TABLE". Each assessing officer is assisted by a Customs Clerk and Postal Staff.

The list of parcels to be opened on a particular day is furnished to the postal department on the previous day. After the parcels are received, assessment is made on the Way Bills (opening the parcels if necessary). The Way bills are returned to the post office with the amount of duty endorsed therein for each parcel.

The parcels are delivered to the addressees by the postman after collection of duty. There is no cash transaction between the Customs and Post Office in regard to duty. The amount of duty collected by the post office is transferred to the Customs Department by book adjustment by the Accountant-General concerned.

If the addressee of a parcel is not satisfied with the assessment made by the Customs Officer, he can ask for reassessment of the parcel. If on reassessment the original assessment is found to be on the high side, then write-back of the amount involved is given and the lower amount is recovered from the addressee.

Gift Articles

Gift articles are also liable to duty unless they are exempt from such duty by a Notification under Section 25 of the Customs Act, 1962. At present bona fide gift parcels excluding alcoholic drinks upto the specified value are passed free of duty in terms of the statutory provisions under Heading No. 9916.00 of the Customs tariff.

Import Trade Control

The restrictions under Import and Export (Control) Act, 1947, and the imports (Control) Order, 1955, as amended applies to post parcel also.

Warehousing of goods without warehousing under Chapter IX

This is an important provision. Sometimes, the goods are held up for clearance by the Customs for some reason or the other and, detention of the goods, ends in accumulation of demurrage charges. These charges are so high these days that when the goods are ultimately released, it is found to equal or even exceeds the duty

assessed. This causes considerable financial strain and hardship to the importers. In order to obviate this contingency, Section 49 of the Customs Act provides that where the Assistant Commissioner of Customs is satisfied, on the basis of an application made by the Importer (or his Agent), that there is likely to be delay in the clearance of the goods, he may permit the goods to be warehoused without attracting the warehousing provisions of Chapter IX of the Act. Once such permission is granted and the goods are transferred to the appointed public/private warehouse, the importer does not incur demurrage charges. He will only have to pay for warehousing the goods, which charges are very nominal.

Bills of Entry—Computerised processing

All importers/exporters, Custom House Agents and other members of the trade are hereby informed that the following additional facilities would be available on the Indian EDI System—Imports with effect from 1st February, 1997:

1. Bills of Entry in respect of the goods which are entitled for the benefit of exemption from special customs duty in terms of Notification No. 77/96, dated 28.9.1996 can be filed electronically. Users may take care to mention the Notification No. correctly to avail of this facility. Remote EDI System (RES- I) users are also advised to get their system duly updated. They may contact the officials of the National Informatics Centre (NIC) in the Custom House for this purpose.
2. Presently, assesses requesting for examination of the goods on their own on first check basis are required to file the Bill of Entry manually. Users of the Indian Customs EDI System - Imports would be able to make a request for first check electronically if it is necessary to do so before assessment and where the complete information is otherwise available for filing the Bill of Entry. In the case of first check at the data entry stage the appropriate column in the Bill of Entry format should be flagged 'y' and the reasons for the request for the first check should also be duly entered. With the introduction of this facility, first check requests will no longer be entertained manually except in cases where the importers do not have any information regarding description/value of goods (Section 46 cases).
3. It has further been decided that with effect from 1.2.1997, Bills of Entry for second hand machinery and motor cars would also be processed on the system. The assessing officers would be giving orders for first check of these goods on the system itself. The procedure thereof would be the same as for other imported goods.

Consequent upon the aforesaid changes, as also the facility of filing of Bill of Entry under the Advance Customs clearance system (introduced vide Public Notice No. 64/96, dated 10.12.1996) the following changes are hereby made in the import declaration form required to be submitted at the service centre as Annexure N to the public Notice No. 28/95 dated 24.4.1995:

- (1) For the existing Sl. No. 12 and the entries relating thereto, the following Sl. No. shall be substituted:

“12. Type of Bill of Entry

A. Home Consumption/Warehousing/ex-bond. B. Advance/post-arrival.”

- (2) For the existing Sl. No. 14 and the entries relating thereto, the following entries shall be substituted:

“14A. Whether first check required; if yes, reasons therefore,

14B. Whether green channel clearance required? (Y/N)”

- (3) In Sl. No. 17, in the table for the heading “Policy para/licence details”, the following heading shall be substituted, namely:

“ITC HS Code/Policy para/Licence details”.

[Commissioner of Customs, New Delhi, Public Notice No. 8/97, dated 20.1.1997].

Bill of Entry - On line noting of procedure

With a view to facilitate speedy clearance of import cargo and simplify the procedures regarding noting of Bill of Entry and data captured on PC-LAN system, Mumbai Custom House has introduced online noting of Bill of Entry.

7.18 Assessable Value and Levy of Duty—Method of Assessment

Customs duty is charged under Section 12 of the Customs Act, 1962. It is leviable on the basis of value or quantity as specified in the Import Tariff (First Schedule) to the Customs Tariff Act, 1985. Value of imported goods as laid down under Section 14 of the Customs Act, includes cost, insurances (including marine and war risk insurance) and freight and also landing charges and stevedoring charges, wherever leviable. Conversion of foreign currency to Indian Currency, for the purpose of arriving at the value in Indian Rupees and levy of duty at ‘ad-valorem’ basis is done with reference to the rate of exchange in force on the date on which the Bill of Entry is presented under Section 46 of the Customs Act, 1962. The rates of exchange for conversion are notified by the Board from time to time as and when the Exchange rates fluctuates. These exchange rates as notified are only applicable notwithstanding the exchange rates that are applied by the Banks in the course of negotiation of documents pertaining to Imports.

(A) Systems of Assessment

There are two systems of assessment: (1) First Appraisalment; and (2) Second Appraisalment.

First Appraisalment means, assessment of goods after the goods are examined. This system is resorted to only in exceptional cases where it is not possible for the Appraiser to determine the value or classification of the goods or for any other reason on the basis of the documents as produced by the importers.

Second Appraisalment means making the assessment on the basis of the declaration made by the importers on the strength of documents such as invoice, catalogue, literature showing the composition and use, price lists, etc., as produced by the importers. Under this system, the goods are examined after assessment and collection of duty.

First appraisal system is goods based assessment and second appraisal system is document based.

Bills of Entry after scrutiny and assessment by the Appraisers are put up to the Assistant Commissioner "in charge of the Group who checks the assessment made". After such a check, the bills of entry are sent to the Comptroller who calculates the amount of duty due at the rates indicated by the Appraiser on the Bills of Entry. After such calculation, the actual amount of duty is typed in "pinpoint" on the Bill of Entry, which is then sent to the "Licence Section" in the Custom House. In the 'Licence Section', the Import licence as filed with the Bill of Entry and accepted by the Appraiser as covering the goods imported, after scrutiny and verification of Import Policy, is screened and registered in the registers maintained for the purpose, and audited.

7.19 Penal Action

In cases where licences are necessary for import of any goods and the importers are not in possession of such licences, the import is held as unauthorised and penal action is called for, for violation of the provisions of Section 3 of the Imports and Exports (Control) Act, 1947, read with Section 11 of the Customs Act, 1962. Penal action is also called for in respect of violations involving mis-declaration of value, description of goods etc., as covered by the various sub-sections of Section 11 of the Customs Act, 1962.

Before any penal action is taken, a show cause notice is issued to the Importer as required under Section 124 of the Customs Act, 1962, asking him to explain as to why the goods should not be confiscated under Section 111 and/or, a penal action taken against him, under Section 112 of the Customs Act, 1962. After getting the Importer's reply and after giving him, a reasonable opportunity to be heard in person if necessary, action is taken to confiscate the goods under Section 111 and penal action taken against him under Section 112 of the Customs Act, 1962. Where the imported goods are confiscated for offences against revenue only, under the provisions of Section 125 of the Customs Act, 1962, normally, an option is given to the Importer to 'redeem' the goods (from confiscation) on payment of (suitable) fine. However, in respect of offences involving "prohibitions or restrictions", such an option for redemption is not given and absolute confiscation of the goods is resorted to. Adjudication of cases is done by the Commissioner (including Additional Commissioner) or Deputy Commissioner or Assistant Commissioner depending on the value limits laid down under Section 122 of Customs Act, 1962, and also subject to the executive instructions. In cases of deliberate attempts of fraudulent evasion of duty, evasion or prohibitions and restrictions tantamount to 'Smuggling', the Importers and all concerned and connected, including the abettors are also liable to be prosecuted under the provisions of Sections 132 to 140 of Customs Act. This prosecution action is independent of departmental adjudication (vide Section 122 of the Customs Act).

After action in the Appraising Department, the Bill of Entry is taken by the importers/agents to the Cash and Accounts Department for payment of duty. The duty can be paid by cash or adjusted in the deposit account maintained with the

Custom House by the Importers, wherein amounts are paid in advance and debits made as and when clearances are to be effected.

After collection of duty, the Accounts Department detaches the original Bill of Entry and returns the duplicate, triplicate and quadruplicate (if filed) to the importers. The duplicate Bill of Entry is taken to the Docks where the imported goods are stored.

7.20 Clearance of Export Cargo

Introduction

International trade is an essential ingredient in the normal economic life of any country. In regard to India, as a developing nation, the need is to achieve favourable balance of payment. Therefore, the trade and industry are to provide positive response to the challenge on the foreign trade front. The Government, on its part, however, with a view to conserve foreign exchange, regulate the 'outflow' of foreign exchange on imports, is restricting imports and encouraging exports with a view to achieving favourable balance of payments position. Despite the whole range of export concessions and incentives being given, the Export performance had not shown considerable improvement in balance of payments. Therefore, the emphatic urge to stimulate exports, is repeatedly being made, with new sets of concessions.

(A) Indian Exports - History

Since independence, India's Exports from "agro-based raw materials and minerals" have shifted to machinery, transport, equipments, electronic gadgets and components, joint-ventures, turn-key projects, etc. Significant changes in the pattern of export trade had taken place and our exports are made particularly to all "permissible destinations". "Export Promotion" as an instrument of policy, in fact, was thought of, during the "Second Five Year Plan Period" and "Export Promotion Directorate" was set up in the Ministry of Commerce, with field formations, in 'port towns' to assist advice and be generally of help to Exporters. Import policy for Registered Exporters was framed during 1969-70, either as a measure of export promotion or with a view to providing against export of specified products, "replenishment from most preferred sources of imported materials for manufacture of export products". Since 1977-78, the entire "Import Policy for Registered Exporters" is undergoing major changes with "bias towards liberalisation" and the Import Policy (1992-97) has lifted all major controls on imports except few in the core sector, to achieve the same. For Export promotion, in short, imports were/are allowed despite indigenous availability in order to ensure that Indian manufactured goods exported are not only goods in terms of quality but competitive in terms of price also.

The recent EXIM policy 2002-07 envisages to capture in global share of trade by 2007 from the present level of 0.67%. This requires an annual growth rate of 12% (compounded). And in dollar terms, the present export business of 46 billion should be increased to atleast 80 billion.

(B) Customs Formalities for Export

While there is very urgent need to promote exports and earn the most needed

valuable foreign exchange/it does not necessarily mean/ that the export goods can be allowed without restriction and/or, without observing any formalities.

Export should be in accordance with rules and regulations to be implemented “at the point of exit” and the authority which can enforce such rules and regulations is the Customs Department.

(C) Statutory/legal provisions in the Customs Act 1962 pertaining to Exports

- (i) The Customs allow imports/exports only through authorised places along the coast/across the land frontier and by air. For this purpose “customs ports”, “customs Airports”, “land customs stations” are notified by the Central Govt. under Section 7(a), (b) and (c) Customs Act, 1962.
- (ii) The master of the vessel should not permit loading of the cargo before ‘Entry Outwards’ is granted by the Customs Department and export cargos can be taken on board the vessel or aircraft or a vehicle (for the land route), only under cover of a duly passed Shipping Bill/Bill of export with the permission of the proper (Customs) officer - (vide Sections 39 and 40 of the Customs Act, 1962).
- (iii) In terms of Section 50 of the Customs Act, 1962 a shipping Bill or Bill of Export (in respect of exports through land route) is to be filed by the exporter or his authorised agent, in the prescribed form [prescribed under Shipping Bill and Bill of Export (Form) Regulations 1976 made under Section 157 of the Customs Act, 1962].
- (iv) The Shipping Bill so filed should be assessed. [The term “assessment” as defined under Section 2(2) of the Customs Act includes assessment to ‘nil’ duty also]. Under Section 18 of the Customs Act, 1962 provisional assessment to duty of goods meant for export is possible under the circumstances indicated in that section. Whenever such provisional assessment is made the provisions of Customs (Provisional Duty Assessment) Regulations 1963 apply. Under Regulation 2 of these regulations, the proper officer shall make an estimate of the duty that is most likely to be levied and if the importer or the exporter as the case may be executes a bond in an amount equal to the difference between the duty that may be finally assessed and the provisional duty and deposits with the proper officer such sum not exceeding 20% of the provisional duty, the proper officer of customs may assess the duty on the goods provisionally at an amount equal to the provisional duty. Where the provisional assessment is allowed pending the production of any document or furnishing of any information by the importer or the exporter, as the case may be, the terms of the bond (in the prescribed form) shall be that such document shall be produced or such information shall be furnished within one month or within such extended period as the proper officer of the customs may allow and the person executing the bond shall pay the deficiency, if any, between the duty finally assessed and the duty provisionally assessed. Where provisional assessment is allowed pending the completion of any test or enquiry, the terms of the bond shall be that the person executing the bond shall pay the deficiency, if any, between the duty finally assessed and the

duty provisionally assessed. The proper officer of customs may require that the bond to be executed under these regulations may be with such surety or security, or both, as he may deem fit.

Thereafter the goods shall be examined physically and permitted shipment by means of passing on the shipping bill a 'Let Export' or 'Let Ship' order. (Sections 17 and 51 Customs Act, 1962).

- (v) The 'assessable value' for export as declared in the shipping bill should be in accordance with the provisions of Section 14 of the Customs Act, 1962. (Declared value is subject to verification as to its correctness or otherwise by Customs authorities).
- (vi) For assessing the goods for export to duty and granting an order of 'Let Export' under Section 51 of the Customs Act, the export goods, should not be "prohibited goods" - prohibited for export under the Customs law or prohibited for export under any other law for the time being in force - The Customs Department in pursuance of Section 11(2)(u) of the Customs Act, 1962 is also empowered to prevent the contravention of any other law noticed in the course of export.
- (vii) Power to confiscate the export goods, "attempted to be improperly exported" etc. has been endowed on the Customs Department under Section 113(a) to (l) of the Customs Act, 1962.
- (viii) Under Section 114 of the Customs Act, "penalty for attempt to export goods improperly", on persons concerned could be imposed (in addition to confiscation of the goods), not exceeding five times the value of the goods.
- (ix) It is also provided in Section 127 of the Customs Act, that award of confiscation and penalty by Customs shall not prevent infliction of any punishment by way of prosecution (in deserving deliberate and grave offences) under Section 132 and 135 read with Section 137 of the Customs Act, 1962.

7.21 Customs Procedure - Documentation for Export

For effecting shipments, the exporter or his agents should file a shipping bill electronically (Section 50 of the Customs Act), (the quadruplicate copy is filed for purposes of Export promotion). These shipping bills could be filed in the Custom House or Air Cargo Complex, 14 days before the arrival of the loading vessel/aircraft. However, the commissioner of customs may, in cases where it is not feasible to make entry by presenting electronically, allow an entry to be presented in any other manner. Steamer agents normally file applications in the custom House in advance of 'grant of Entry outwards' of the vessel. In the application they furnish, the particulars of the vessel viz. Name, Nationality, Tonnage, the port for which the vessel will load cargo, the nature of cargo, etc. Immediately on presentation of the application, a number called 'Rotation No.' (Export Manifest No. or Export General Manifest No.) is assigned. After the compliances of the above requirements the exporters or their agents may present the shipping bills for the export of their goods. Subsequently, after arrival of the vessel and when she is about to start loading export cargo, orders for 'Entry Outwards' are given by the Customs Authorities. In terms of Section 39 of the Customs Act, the person in charge of the vessel should not allow

loading of cargo before the grant of Entry outwards. The facility afforded to the intending Exporters to file shipping bills immediately after the filing of "Application for Entry outwards" by steamer agents, which is normally done 14 days ahead of the arrival of the vessel, is to enable the exporters to complete all the customs formalities and keep the goods ready for loading.

(a) Documents to be filed along with the Shipping Bill

1. G.R. form in duplicate in respect of exports to all countries except Afghanistan and Pakistan.

Note: To Pakistan and Afghanistan - EP forms in triplicate are to be prepared in lieu of GR forms and are to be filed along with the shipping bill, with the approval of the Reserve Bank of India.

(b) Procedure for obtaining GR Form from Reserve Bank of India through Banks dealing in Foreign Exchange — Authorised dealers in Foreign Exchange

1. Every person/firm/company engaged in Export Business should obtain an Exporter Code Number from RBI. For this, application, in duplicate in the prescribed form called CNX should be made to the Exchange Control Department/ RBI/ through the bankers of the applicant and application (in duplicate) should be made only by the Head/Principal office of the firm/company along with the allotment of "Permanent A/C No." (PAN) from the Income Tax Deptt. The RBI would allot the code number and there is no need to renew or revalidate the same once the no. is allotted. The Number should be cited invariably in the Export forms used for declaration of Exports (GR forms). Customs Authorities will not entertain any Export form/ which does not bear the Exporter Code Number allotted by the RBI. The Code Number allotted to the applicant by RBI is intimated to them on the copy of form CNX (Application Form) submitted by the applicant.

Immediately on allotment of the Code Number the applicant, Bank dealing in Foreign Exchange would supply GR Forms. These forms are printed and supplied by RBI to the Banks. These bear serial numbers and bear also indications as to the stations from where they are issued. The RBI keeps a watch over the disposal of GR forms by Banks *vis-a-vis* repatriation of export sale proceeds by the Exporters as shown in the forms. The GR forms should be completed by the Exporter "in duplicate" and should be presented to the Customs along with the Shipping Bill. Shipping Bill presented without GR forms will not be accepted by Customs unless such non-filing of the GR form is waived by the RBI. In fact export without GR forms will be treated as unauthorised Exports by customs and the goods will be liable to confiscation.

2. Four copies of Export Invoices/ indicating all particulars such as, the number of packages, quantity, unit price, full description of the goods value in total, CIF; FOB or C&F, as the case may be.

3. Packing List.

4. Export Contract; Letter of Credit and all connected correspondence.

5. Inspection/Examination certificates from Agmark grading authorities in respect of agricultural commodities.

6. Pre-shipment and compulsory quality control certificates in respect of goods covered under the compulsory quality control and pre-shipment inspection scheme (under the Export (Quality Control and Inspection) Act, 1963).

7. Export Trade Control licence is issued by the office of the Joint Chief Controller of Imports & Exports in respect of goods that are listed under Schedule I-Part B (Export Policy 88-91) under clause 3(1) of the Export (Control) order, issued in pursuance of Section 3(1) of the Imports and Exports (Control) Act, 1947. Normally the Licence from Export Trade Control Authorities of the office of the Joint Chief Controller of Imports and Exports' is endorsed on the shipping Bill itself. Officers of the abovesaid formation are stationed along with customs officers in major ports/ Air Cargo complexes and the Shipping Bills are routed through them before being presented to the Customs. In fact, Licence endorsements made by them on the Shipping Bills wherever required have been defined as "Licence' under clause 2(d) of the Exports (Control) Order, 1977. It is stated that "Licence" (in the above regard) includes "a licencing endorsement made on a shipping Bill". Separate licences are also issued by the Licensing Authorities with validity for a period of 6 months. "Licence' given in the form of endorsements on Shipping Bill is valid for a period of 15 days at a given time from the date of issue.

8. ARE-1 or ARE-2 as applicable under Rules 18 or 19, Central Excise Rules, 2002 Forms (Application for Removal of Excisable Goods for Export) in duplicate duly completed in all respects for the export of excisable goods.

9. In regard to 'handicraft exports' items which fall under the category "India items" e.g.. wall hangings/woolen carpets/mirror or bidriware/ etc. should be covered by a certificate issued by All India Handicrafts Board.

10. Garments and Textile for their export, should be validly covered by an "Inspection Certificate" from the Textile Committee. In addition, for export to USA "visas" should also be endorsed by the Textile Committee in the format "Special Customs Invoice".

11. GSP Certificate issued by the respective Inspection and/ or promotion councils depending upon the nature of goods for exports to west European countries/ USA/Australia and New Zealand.

In addition, the exporter should make and subscribe to a declaration at the bottom of the copies of shipping Bills as to the truth of the contents, in terms of Section 50(2) of the Customs Act, 1962; Section 13 of the Export (Control) Order, 1977 and Section 20 of the Foreign Exchange Management Act, 1999.

(c) Kinds of Shipping Bill

There are four categories of shipping bills viz. those

- (i) for Free goods;
- (ii) for Dutiable goods, assessable to duty and/or cess;
- (iii) for shipment under claim for drawback (Green Shipping bill); and
- (iv) for shipment from bond i.e., 'Ex-bond'.

(d) Action taken on the shipping bill filed

The shipping bills along with the above detailed documents on presentation in the Export Documentation Centre at the sea port or at the Airport are assigned Sl. Nos. and stamped (admitted) with date of receipt. The Appraiser (proper officer) of Customs checks—

- (i) that the shipping bill has been filed in a reasonably complete form, duly signed by the exporter and the Custom House Agents.
- (ii) that the declarations made on the shipping bill and the truth of such declarations as subscribed by the signature of the exporter and custom House Agents are duly supported by the documents, that are filed along with the shipping bills.
- (iii) that the value (Full export value) declared in the GR form is correct with reference to export contract and connected documents that are filed and are called for.
- (iv) the correctness or otherwise of the value declared on the shipping bill under Section 14 Customs Act with reference to documents filed by making market enquiries, if warranted.
- (v) that various prohibitions and restrictions envisaged under the Customs Act, Imports and Exports (Control) Act, (Export Policy) and the relevant provisions of the other Allied Acts, are not contravened in regard to such exports.
- (vi) the goods are properly classified for collection of export duty (under Second Schedule to Customs Tariff Act, 1985 – Export Tariff) and Cess (under Cess schedule) as the case may be, by indicating the rates there against. The Export Tariff is a selective Tariff and contains only 25 items. Articles not covered by any of these 25 items are not leviable to Export duty. Even in respect of these 25 items, the effective rate of duty has to be determined with reference to ‘exemption notifications’ issued under Section 25 of the Customs Act. Thus, very few items are actually liable to duty on export. The purpose/intention of the Government in having a “selective tariff” on the Export side is not to burden the Export goods with “duty” which would/may render them, not competitive, to whatever little extent, in foreign markets. Export duty is, therefore, levied and collected mostly on items in respect of which India enjoys a sellers market.

Commodities, as enumerated in the Cess Schedule, which forms part of the Customs Tariff (Working Schedule) attract cesses under various enactments (as detailed thereunder). Most of the commodities mentioned in the cess schedule require levy of cess at 1/2% ad-valorem (in addition to Export duty wherever export duty in respect of the commodity is leviable). In respect of some of the commodities “tariff values” are fixed by the Ministry (as indicated in the cess schedule) with effect from the first July of every year. In such cases/ the cess is calculated on the “tariff value” irrespective of the “invoice value”.

The assessable value of Export goods leviable to ad valorem duties (other than tariff valued items) is always the FAS (Free Alongside) values. In the shipping Bill this is indicated as "Real Value" also. This is derived from the contract value or the price contracted upon for export, between the Indian Exporter and the Foreign buyer. If the contracted price is anything other than FAS, then the value for customs purposes-FAS (the price for delivery at the place of Exportation - Section 14 of the Customs Act, 1962) is arrived at and duty is calculated on the FAS value so arrived at.

- (vii) After valuation, classification and assessment of goods, the Appraiser gives directions on the reverse of the duplicate copy of the shipping bill for opening and examination of the consignment physically before permitting the goods to be taken on board the vessel or aircraft. The directions to carry out examination in a particular manner are given in such a manner causing verification to be made with reference to the details of declaration(s) made on the shipping bill and other documents vis-a-vis the actual goods tendered for export and to ensure that quality controls are implemented.
- (viii) On completion of the above, the original copy of the Shipping Bill and the original copy of the GR Form are detached. Physical examination of the goods, permitting the goods for Shipment by the Appraisers and actual physical supervision of shipment of the goods as covered by Shipping Bill are carried out by the Proper officers, on duplicate and triplicate copies of Shipping Bills respectively, and on the basis of the duplicate copy of the GR forms. On completion of shipment, the Proper officers make suitable endorsements on the above documents as to the fact of the goods having been shipped.
- (ix) If the Examination of the goods show that the contents are in accordance with the declarations, then the shipments will be permitted, as otherwise they will not be permitted for shipment and will be detained by the department for further action such as, confiscation, levy of penalty, etc., as the case may need, under Sections 113 and 114 of Customs Act, 1962 respectively,

7.22 Shipment (Export) under claim for Drawback

The term 'drawback' is applied to certain amount of duties of customs, sometimes the whole, sometimes only a part, paid back by Government on the exportation of commodities on which they were levied. To entitle goods to drawback, they must be exported to a foreign port, the object of the relief afforded by the drawback being to enable the goods to be disposed of in the foreign market as if they have never been taxed at all.

For Customs purposes "drawback" means the refund of custom duty and the Central Excise duty that are chargeable/charged on imported and indigeneous materials used in the manufacture of goods exported.

From the point of view of "Export Promotion" it is a relief of duty given to exporters, both manufacturer and merchant exporters.

There are two categories of materials which are used in the manufacture of goods exported, namely imported and indigenous. Consequently, drawback is to be paid in respect of two types of duties: Import duty and Excise duty.

The provisions relating to drawback are enumerated in Chapter X, Sections 74 to 76 of the Customs Act, 1962. Of these, Section 75 deals with the payment of “drawback on Imported materials used in the manufacture of goods which are exported”.

Under Section 75(2) of the Customs Act, 1962, the Central Government is empowered to make rules for payment of drawback and such rules provide:

- (a) for the payment of drawback equal to the amount of duty paid on the Imported materials used in the manufacture of goods or as is specified in the rules as the average amount of duty paid on the materials of that class or description of goods either by manufacturers generally or by any particular manufacturer.
- (b) for the production of such certificates documents and other evidence in support of each claim of drawback, as may be necessary etc.

The rules made in this regard, read with Section 37 of the Central Excise Act, 1944 are called “The Customs and Central Excise Duties Drawback Rules, 1995.

Claim for drawback — Exporters declarations and documents

In terms of the above said rules at the time of export of the goods the exporter *inter alia* shall:

- (i) File a Shipping Bill “under claim for Drawback”. (Green Shipping Bill)
- (ii) State in the above said Shipping Bill, the description quantity and such other particulars as are necessary for deciding whether the goods are entitled to drawback and if so at what rate or rates.
- (iii) File the documents as enumerated already and the Customs formalities to be completed for shipment are the same as detailed above in respect of goods shipped under claim for drawback also under cover of a “Green Shipping Bill”.

On completion of shipments the drawback claimed on exports is scrutinised in the drawback department or the drawback unit of the Custom House or Air Cargo Complex and payments are made by cheques drawn in favour of banks as nominated by Exporters.

7.23 Procedure for Exports through inland Container Depots

(i) Introduction

Shipping is the cheapest way to transport goods. The cost per mile of water borne cargo is half the cost of any other form of long distance transport. Cargo comes in all shapes and sizes.

Each item of cargo must be individually arranged, counted, handled and put on board the ship according to a detailed cargo plan. This involves time and man-power and is costly. Therefore, it is quicker and cheaper to have cargo of a standard shape and size which is easy to handle and stack. Such a cargo type is termed a “Unit load” which in transportation usually means a “container”.

(ii) Evolution

In response to “Cost cutting” and “time saving” requirements of modern trade “containerisation” has come about in the past decade. This system was introduced in “sea transport” in 1949 when John Wollan sent a “box” of sports goods across Irish sea. The “white pass and Yukon route” introduced deep sea container traffic from Canada and the world’s first fully integrated container service came into being in 1955. The world’s largest container shipping service was founded in USA-Malcolm Mc Clean Service.

A modified version of ‘containerisation arose in 1968. It is known as “Lighter” aboard ship”- FLASH. In the flash system, lighters are loaded on the shore and floated out to the ship waiting off-shore. The ship lands the lighters on board with its own crane (Gantry crane) and stacks them there high like containers. At the port of arrival the lighters are unloaded and floated to shore. This saved/saves both port costs and cuts time spent waiting for an empty berth.

(iii) Conventional cargo ships vis-a-vis container ships

Conventional cargo ships are not being swept away from the seas by containerisation. Only on certain busy routes as the North Atlantic run/ has the switch over to containers been near complete. Elsewhere, the conventional cargo, ship has maintained its hold. For a small port handling a few thousand tonnes of cargo, it does not make economic sense to instal a container berths handling equipment and road and rail connections. Conventional cargo ships are helped by the fact that not all cargoes will economically containerise. Such cargoes are usually large (logs for instance) or heavy (steel plates). Another requirement in respect of containers is that for “every box” at sea another three are needed on land; one at the port of departure, one at the port of arrival and one being repaired.

(iv) What is a Container ?

A container is simply a box. It is no more complex than a truck body, a railway freight van or a ship’s hold. Containers are made of aluminium, steel, fibre glass or plywood for lightness with steel frames to give strength. Standard sizes for containers are 40, 20, or 10 feet long, 8ft. wide and 8ft. in height. Some have open tops or sides for loading special cargo. Liquids are carried in boiler shaped tanks surrounded by rectangular frame work. Other containers are insulated or refrigerated and are constructed according to International standards and inspected by Insurance companies.

(v) How are they loaded on the ship

Container ships are built in vertical cells. The container slips into position in each cell down guide rails. The containers sit on the top of each other in the ship’s hold. Container ships towards insuring loss over board, are designed with distinctive concave low shapes to keep waves clear of the decks.

(vi) Handling of containerised cargo in India

In India, procedures have been drawn up for handling containerised cargo both on the Import and Export side. The Import and Export Cargo

containerisation presupposes formation of Inland Container Depots and should have the necessary arrangement and infrastructure of rail and road connections.

Inland Container Depots can be opened or can come up only in places which are appointed places for unloading of Imported goods and the loading of Export goods or any class of such goods by Central Government, by notification in the official gazette as contemplated under Section 7 of the Customs Act, 1962. In the Southern Region, Bangalore, Coimbatore and Anaparte (near Guntur) have been declared as I.C.Ds.

(vii) Categories of Containerised Cargo

Containerised Cargo is divided into two categories viz. Full Container Load (FCL) and Loose Container Load (LCL). By FCL, it is understood that the entire cargo in a particular container belongs to a single consignee of a particular port, place, while LCL denotes container containing several consignments (Break Bulk) belonging to various consignees of a particular port/place.

(viii) Short shipment Notice

In the event of the Export goods passed for shipment, not shipped (shut out) or short shipped, Short Export Rules, 1963, framed in exercise of powers conferred on the Central Government, under Section 156 Customs Act, 1962, require information of short shipment non-shipment (shut out) to be given to the customs department before the expiration of 7 days from the date of the departure of the vessel. Failure to comply with this provision entails penalty not exceeding ₹100/-.

No particular form for intimating short shipment or non-shipment (shut out) of goods has been "prescribed" as "form of Notice" under Short Export Rules. But for the convenience, the trade has been notified to file such notices in Triplicate with the required particulars in Annexures 'A' and 'B' to this study.

On receipt of Short-shipment/non-shipment (shut out) notices, the Customs Department returns one copy to the Exporters or to their agents duly acknowledging the receipt of the notice; sends one copy to Reserve Bank of India who are policing the repatriation of Export sale proceeds from abroad, as declared on the GR form and the third copy is connected to the relative Shipping Bill in the Export Manifest of the vessel filed by the Steamer agents. One Short shipment/non-shipment notice is required to be filed for each Shipping Bill. Failure to comply with the above requirement, apart from causing inconvenience to the Exporters, in explaining the short realisation of the export sale proceeds to the Reserve Bank of India, at the appropriate time, will render the Exporters and/or their agents liable for penal action under Rule (3) of the Short Export Rules, 1963.

(ix) Amendment application in lieu of Short Shipment Notices

In the event, the goods covered by a Shipping Bill have been "shut out" in full, the Shippers/Exporters are allowed to amend the ship's/vessel's name on the shipping bill, when the new ship had "entered outwards" in the port,

and ship the goods. This can be done provided the period allowed under the notice of Short Export Rules, 1963 (viz. 7 days) had not lapsed.

7.24 Procedure for Exports of Containerised Cargo from Inland Container Depots

The exporters file shipping bills at the I.C.D. The Shipping Bills will be filed in five copies, original, duplicate, triplicate and two transference copies which are in distinct colors for easy identification and handling. The documents that are to be filed along with the shipping bills are as detailed earlier. In addition to the usual information given on the shipping bills the exporters should mention the Port of Exit and the serial number of the containers. Each container will have different marks and numbers.

Classification and assessment will also be completed at the I.C.D, following usual prescribed checks and formalities as detailed already. The original shipping bill will be retained and the other copies handed over to the exporters for completion of examination and other formalities.

The exporters will submit alongwith the shipping bills the set of G.R. forms (original/duplicate). The "Full Export Value" will be verified as usual on the G.R. Form; original copy of G.R. will be detached at the I.C.D. and will be sent direct to the Reserve Bank of India. The duplicate copy of the G.R. form will be handed over to the exporter alongwith the shipping bills.

The export goods, will be presented to the 'Customs Officer in the "I.C.D. alongwith the Shipping Bills". The examination will be conducted in accordance with the procedure prescribed for examination of export goods after which the goods will be allowed to be "stuffed" into the containers under Customs supervision. The quantity of goods loaded (number of packages etc. shut out) will be recorded on the shipping bill. Once the goods are loaded into the container, the containers will be sealed with "one time lock" containing identification details as supplied by the Railway and record maintained for the same with the I.C.Ds. Simultaneously, with the stuffing of the goods inside the containers, the exporters will prepare in quadruplicate, the invoices and container-wise packing weight specifications indicating *inter alia* the number of packages (with marks and numbers, if any), description and total quantity, net weight/packed in each container along with the corresponding shipping bill number. The Customs officers will certify these details on the invoice/packing list. Duplicate copy of the shipping bill will be retained in the I.C.D. and triplicate handed over to the exporter.

The two transference copies of the Shipping bills will be placed in a sealed envelope and handed over to the carriers (Railways) who will be responsible for its being carried alongwith the container and its production to the Customs officer at the port of exit.

At the exit Ports the containers will be allowed to be exported under customs (preventive) supervision on checking of the seals without any further examination (examination will only be done if the seals of the containers are found to have been tampered with or on the basis of any information, doubts etc.) The Preventive officer who will be supervising the loading of the containers will suitably endorse the two transference copies of the shipping bills regarding the fact of shipment.

At the Port of Exit, the Steamer Agents will also file the export manifesto in duplicate regarding the containerised cargo in the 'container cell' to the Preventive Department of the respective Custom House. After shipment of the goods, one transference copy of the shipping bill will be returned to the respective I.C.D.

The Export Manifest transference copies of the shipping Bill and the weekly statement received from the Custom House (Exit ports) will be correlated for finalisation of drawback claims/ Closure of export manifest, etc. at the ICD.

7.25 Baggages

Chapter XI of the Customs Act, 1962 contains special provisions regarding baggage, goods imported or exported by post and stores. This Chapter is divided into three Parts, Part I dealing with baggage, Part II with goods imported or exported by post, and Part III with Stores. Sections 77 to 81 are in Part I, Sections 82, 83 and 84 form part II and Sections 85 to 90 form Part III of Chapter XI. Chapter XII of the Act deals with provisions relating to coastal goods and vessels carrying coastal goods. These provisions are discussed hereinbelow:

Declaration by Owner of Baggage

Section 77 provides that the owner of any baggage shall for the purpose of clearing it make a declaration of its contents to the proper officer.

The word 'baggage' is a comprehensive term which means luggage of a passenger accompanied or unaccompanied and comprises of the trunks or bags and the personal belongings of the passenger contained therein. It is in this comprehensive sense that the term "baggage" has been used in Sections 77 and 80 of the Customs Act. Thus, 'baggage' has been given a larger and ordinary meaning. (*Union of India v. Khalil Kecherim*, 1970 Cri. L.J. 417).

Section 2(3) of the Customs Act defines baggage as including unaccompanied baggage but excluding motor vehicle.

Determination of Rate of Duty and Tariff Valuation in Respect of Baggage

According to Section 78 of the Customs Act, 1962, the rate of duty and tariff-valuation, if any, applicable to baggage shall be the rate and valuation in force on the date on which a declaration is made in respect of such baggage under Section 77.

Bona-fide Baggage Exempt from Duty

Section 79(1) provides that the proper officer may, subject to any rules made under Sub-section (2) pass free of duty —

- (a) Any article in the baggage of a passenger or a member of the crew in respect of which the said officer is satisfied that it has been in use for such minimum period as may be specified in the rules.
- (b) Any article in the baggage of a passenger in respect of which the said officer is satisfied that it is for the use of the passenger or his family or is a bona-fide gift or souvenir.

Provided that the value of each such article and the total value of all such articles does not exceed such limits as may be specified in the rules [Section 79(1)].

The Central Government may make rules for the purpose of carrying out the provisions of this section and in particular, such rules may specify -

- (a) the minimum period for which any article has been used by a passenger or a member of the crew for the purpose of clause (a) of Sub-section (1).
- (b) the maximum value of any individual article and the maximum total value of all the articles which may be passed free of duty under clause (b) of Sub-section (1).
- (c) the conditions (to be fulfilled before or after clearance), subject to which any baggage may be passed free of duty. [Section 79(2)].

Section 79(3) lays down that different rules may be made under Sub-section (2) for different classes of persons.

In the Act a distinction has been made between 'baggage' and 'bona-fide baggage' which is exempt from customs duty and in respect of which the proper officer has been empowered to pass free of duty any article which is in the baggage of a passenger and which has souvenir. Therefore, any article in the baggage of a passenger, even though it may be 'goods' within the meaning of Section 2(22) of the Act, will be allowed to be imported free of duty, if it is passed under Section 79 of the Act.

The Government of India in the Ministry of Finance, Department of Revenue and Excise has in exercise of powers conferred by Sub-section (2) of Section 79 framed the Baggage Rules, 1998, the Tourist Baggage Rules, 1998 and the Transfer of Residence Rules, 1978. The text of these rules is given in Annexure 1 to this Study.

7.25.1 Temporary Detention of Baggage

Section 80 of the Customs Act, provides that, where the baggage of a passenger contains any article which is dutiable or the import of which is prohibited and in respect of which a true declaration has been made under Section 77, the proper officer may at the request of the passenger, detain such article for the purpose of being returned to him on his leaving India.

7.25.2 Regulation in respect of Baggage

Section 81 lays down that the Board may make regulations:

- (a) providing for the manner of declaring the contents of any baggage;
- (b) providing for the custody, examination, assessment to duty and clearance of baggage;
- (c) providing for the transit or transshipment of baggage from one customs station to another or to a place outside India.

Budget 2002 enhanced limits for the residence transfer for those shifting residence to India. The persons shifting residence to India can avail concessional rate of 15% duty on the baggage upto the following limits as follows:

Mini transfers

2001 Budget	upto ₹ 30,000
2002 Budgets	Extended upto ₹ 75,000

Major transfers

2001 Budget	₹ 1.25 lakh
2002 Budget	₹ 5 lakh

It may be noted that now items like laptop, portable photocopies etc. are also allowed at concessional rates.

Normal rate for baggage is 150% (CVD and SAD) exempt but the effective rate is 35%.

Cesses will be payable at applicable rates.

7.26 Goods Imported or Exported by post

As already stated, Sections 82 to 84 deal with goods imported or exported by post. These provisions are discussed hereinbelow:

(a) Label or Declaration accompanying Goods to be treated as Entry

Section 82 of the Act lays down that in the case of goods imported or exported by post any label or declaration accompanying the goods which contains the description, quantity and value thereof shall be deemed to be an entry for import or export, as the case may be for the purpose of this Act.

(b) Rate of Duty and Tariff Valuation in respect of Goods Imported or Exported by Post

Section 83(1) lays down that the rate of duty and tariff value, if any, applicable to any goods imported by post shall be the rate and valuation in force on the date on which the postal authorities present to the proper officer a list containing the particulars of such goods for the purpose of assessing the duty thereon, provided that if such goods are imported by a vessel and the list of the goods containing the particulars was presented before the date of the arrival of the vessel, it shall be deemed to have been presented on the date of such arrival.

Section 83(2) lays down that the rate of duty and tariff value, if any, applicable to any goods exported by post shall be the rate and valuation in force on the date on which the exporter delivers such goods to the postal authorities for exportation.

(c) Regulations Regarding Goods Imported or to be Exported by Post

The Board may make regulations providing for —

- (a) the form and manner in which an entry may be made in respect of any specified class of goods imported or to be exported by post, other than goods which are accompanied by a label or declaration containing the description, quantity and value thereof.
- (b) the examination, assessment to duty, and clearance of goods imported or to be exported by post.

- (c) the transit or transhipment of goods imported by post from one customs station to another or to a place outside India (Section 84).

In exercise of powers conferred under Section 84, the Central Board of Revenue has made the following rules for the landing and clearing at the ports of Bombay, Calcutta, Madras, Dhanushkodi and all the Land Customs Stations and Airports of parcels, and packets forwarded by the foreign mails or by passenger vessel or air lines.

(d) Postal Parcels and Letter Packets from Foreign Ports out of India

(i) Landing

- (1) The boxes or bags containing the parcels be appropriately labelled e.g., "Postal Parcels" ("Colist Postaux") "Parcel Post". "Parcel Mail", "Letter Mail" and as such will be allowed to land pass, either with or separately from the regular mails, at the Foreign Parcel Department of the Government Post Offices in case of ports of Calcutta and Madras, at the Foreign Parcel Department of the Foreign Post in the case of the port of Bombay and the Foreign Parcel Department of Office at Madurai in the case of the port of Dhanushkodi, at the Sorting Air Mail Office at Delhi and the office of Foreign Post at New Delhi in the case of airports of Delhi and at the Foreign Parcel Department of Golakganj in the case of the Land Customs Station at Golakganj in Assam.

(ii) Clearing

- (2) (a) The Postmaster shall, on receipt of the parcel mail, hand over to the Principal Postal Appraiser (a) a memo showing the total number of parcels received by that mail from each country of origin, (b) parcel bills (in triplicate) in the form approved by the Chief Customs Officer, or the senders' declarations and any other relevant documents that may be required for the preparation of the parcel bills by the Customs Department, (c) the relative Customs declarations and despatch notes (if any), and (d) any other information required in connection with the preparation of the parcel bills which the Post Office is able to furnish.
- (b) The Postmaster shall, on receipt of letter mail bags and in consultation with the Principal Postal Appraiser get the bags opened and scrutinised under the supervision of the Customs Appraiser with a view to detain all packets suspected to contain dutiable articles. The packets thus detained will be presented in due course to the Customs Appraiser with letter mail bill and assessment memos for assessment as per rule (6)(b).
- (3) On receipt of those documents, the Customs Appraiser shall scrutinise the particulars given therein and shall mark off on the relative declarations on parcel bills, as may from time to time be directed, all parcels required to be detained for examination either for want of necessary particulars or defective description or suspected misdeclaration or undervaluation of contents. They shall assess the remaining parcels by showing the rates of duty on the declarations or parcel bills, as the case may be. For this

purpose, they will generally be guided by the particulars given in the parcel bills or Customs declarations and despatch notes (if any). When any invoice, document or information is required whereby the real value, quantity or description of the contents of, a parcel can be ascertained, the addressee may be called upon to produce or furnish such invoice, documents and information.

- (4) The Customs clerk shall then transcribe on to the parcel bill whenever necessary the values from the declarations and after converting them into Indian currency at the ruling rates of exchange shall calculate and enter the amount of duty. The parcel bills with the declaration so completed, shall then be audited by the Audit clerks and the original and duplicate copies shall be returned to the Postmaster with as little delays as possible, the triplicate being retained in the Customs Department.
- (5) The Postmaster shall then detail all parcels marked for detention in the manner indicated above, and shall allow the rest to go forward for delivery to addressee on payment of the duty marked on each parcel.
- (6) (a) As soon as the detailed parcels are ready for examination, they shall be submitted together with the parcel bill to the Customs appraisers who, after examining them and filing in details of contents of value in the parcel bills, will note the rate and amount of duty against each item. The remarks "Examined" shall be entered by the Appraiser against the entry in the parcel bill relating to each parcel examined by him. The parcel bill shall then be audited and the original and triplicate copies returned to the Postmaster, the duplicate being retained in the Customs Department.
- (b) As soon as packets detailed as per rule (2)(b) are ready for examination and assessment, they shall be submitted together with the relative letter mail bill and assessment memos to the Customs Appraising Officer who, after examining them and filling the details of contents of value in the bill, will note the rate and amount of duty against each item. He will likewise, fill in these details on the assessment memo, to be forwarded along with each packet. The bill and the assessment memo shall then be audited.
- (7) All parcels or packets required to be opened for Customs examination shall be opened, and after examination re-closed by the Post Office officials and shall then be sealed by them with a distinctive seal. The parcels or packets will remain throughout in the custody of the Post Office officials, but if it comes to the knowledge of the Appraiser at the time of examining any parcel or packet that its contents are damaged or short, a note thereof shall be made on the parcel or packet bill.
- (8) If on examination the contents of any parcel or packet are found to be misdescribed or the value understated or to consist of prohibited goods, such parcels or packets shall be detained and reported to the Customs Commissioner, and the Postmaster shall not allow such parcels or packets to go forward without the Customs Commissioner's orders.

- (9) The duties as assessed by the Customs Appraiser and noted in the parcel bill or letter mail bill shall be recovered by the Post Office from the addressees at the time of delivery to them. The credit for the total amount of duty certified by the Customs Appraiser at the end of each bill shall be given by the Post Office to the Customs Department in accordance with the procedure settled between the two Departments from time to time.
- (10) The duties imposed by these rules upon Customs Appraisers shall be performed at Madurai by such officer as the Chief Customs Officer may determine.
- (11) The parcel bills or letter mail bills and other document on which assessment is made shall remain in the custody of the Post Office, but the duplicates, where these are prepared, shall be kept in the Customs Department for dealing with claims for refunds, etc., and shall be preserved for three years.

The parcel bill or letter mail bill shall show the following particulars:

- (a) Number assigned by office of posting.*
- (b) Name of office of posting.*
- (c) Name of office of destination.*
- (d) Weight of insured parcels.*
- (e) Local number.*
- (f) Contents as ascertained by the Customs.*
- (g) Declared value in foreign currency.*
- (h) Rupee value.*
- (i) Rate of duty.*
- (j) Amount of duty.*

Postal Parcels or Packets from Foreign Ports in India

- (12) Postal parcels or packets from foreign ports in India may be forwarded as ordinary mails to the Foreign Parcel Department of the General Post Office.
- (13) For assessment and other Customs purposes such parcels will be treated in the same manner as postal parcels from foreign ports out of India and the procedure prescribed in Rules (2) to (10) above shall be followed.

7.27 STORES

Sections 85 to 90 deal with Stores i.e. goods which are supplied as Stores to the vessels or aircrafts. These provisions are as follows:

(a) Stores may be allowed to be warehoused without assessment to duty

Where any imported goods are entered for warehousing and the importer makes and subscribes to a declaration that the goods are to be supplied as stores to vessels or aircraft without payment of import duty under this Chapter (i.e. Chapter XI) the proper officer may permit the goods to be warehoused without the goods being assessed to duty (Section 85).

(b) Transit and Transshipment of Stores

Any stores imported in a vessel or aircraft may without payment of duty, remain on board such vessel or aircraft while it is in India. [Section 86(1)].

Any stores imported in a vessel or aircraft may with the permission of proper officer be transferred to any vessel or aircraft as stores for consumption therein as provided in Section 87 or Section 90 [Section 86(2)].

In exercise of the powers conferred under Section 86, the Central Board of Revenue has made the Imported Stores (Retention on Board) Regulations, 1963 According to these regulations, any imported stores on board a vessel arriving from a foreign port or an aircraft arriving from a foreign airport may remain on board such vessel or aircraft without payment of import duty leviable thereon during the period such vessel or aircraft is not a foreign-going vessel or aircraft, subject to the condition that where such stores are consumable stores:

- (a) in the case of alcoholic liquor, cigarettes, cigars and pipe tobacco, such stores are kept under Customs seal:
- (b) in the case of consumable stores other than those specified in clause (a) such of other stores are likewise kept under Customs seal.

Provided that if the proper officer is satisfied that it is not practicable so to do, he may, after taking inventory of such stores, allow them to remain on board without being put under Customs seal. Where any stores have been kept under Customs Seal, such seal shall not be broken until the vessel or aircraft becomes a foreign-going vessel or aircraft.

(c) Imported Stores may be Consumed on Board a Foreign going Vessel or Aircraft

Any imported stores on board a vessel or aircraft (other than stores to which Section 90 applies) may without payment of duty be consumed thereon as stores during the period such vessel or aircraft is a foreign-going vessel or aircraft. (Section 87).

The Central Board of Excise and Customs has made the Bonded Aircraft Stores (Procedure) Regulations, 1965 which provide for the following:

(d) Warehousing of goods for use as stores

- (1) Where any imported goods for use in a foreign-going aircraft are to be entered for warehousing under Section 85 of the Act, an application in Form I shall be made to the Assistant Commissioner of Customs.
- (2) Every such application shall be deemed to be the Bill of Entry in relation to the goods supplied specified in that application for the purpose of Section 46 of the Act.
- (3) On receipt of an application under Sub-regulation (1), the Assistant Commissioner of Customs may permit the goods specified in that application to be warehoused without the goods being assessed to duty.

(e) Clearance of Warehoused Goods for Supply as Stores in a Foreign going Aircraft

- (1) Where goods permitted to be warehoused under sub-regulation (3) of regulation 3 (above) are to be cleared for use as stores in a foreign-going aircraft, an application shall be, made to the Assistant Commissioner of Customs in Form II.
- (2) Every such application shall be deemed to be the shipping bill in relation to the goods specified in that application for the purpose of Section 50 of the Act.
- (3) On receipt of an application under Sub-regulation (1) the Assistant Commissioner of Customs may permit the clearance of the warehoused goods specified in that application for being taken on board the foreign-going aircraft as stores in accordance with the provisions of Section 69 of the Act as applied to stores by Section 88 of the said Act.

(f) Application of Section 69 of Chapter X to Stores

Section 88 provides that provisions of Section 69 and Chapter X shall apply to stores (other than those to which Section 90 applies) as they apply to other goods, subject to the modifications that:

- (a) for the words, "exported to any place outside India" or the word "exported" wherever they occur, the words "taken on board any foreign-going vessel or aircraft as stores" shall be substituted.
- (b) in the case of drawback on fuel and lubricating oil taken on board any foreign-going aircraft as stores. Sub-section (1) of Section 74 shall have effect as if for the words "ninety-eight per cent" the words "the whole" were substituted.

(g) Stores to be Free of Export Duty

Goods produced or manufactured in India and required as stores on any foreign-going vessel or aircraft may be exported free of duty in such quantities as the proper officer may determine having regard to the size of the vessel or aircraft, the number of passengers and crew and the length of the voyage or journey on which the vessel or aircraft is about to depart (Section 89).

(h) Concession in respect of imported stores for the Navy

Section 90(1) provides that, imported stores specified in Sub-section (3) may without payment of duty be consumed on board a ship of the Indian Navy.

Section 90(2) lays down that the provisions of Section 69 and Chapter X shall apply to stores specified in Sub-section (3) as they apply to other goods, subject to modification that:

- (a) for the words "exported to any place outside India" or the word "exported" wherever they occur, the words "taken on board a ship of the Navy" shall be substituted.

- (b) for the words, “ninety-eight per cent” in Sub-section (1) of Section 74, the words “the whole” shall be substituted.

The stores referred to in Sub-sections (1) and (2) are the following:

- (a) Stores for the use of a ship of the Indian Navy;
- (b) Stores supplied free by the Government for the use of the crew of a ship of the Indian Navy in accordance with their conditions of service [Section 90(3)].

7.28 Provisions Relating to Coastal Goods and Vessels Carrying Coastal Goods

Chapter XII deals with provisions relating to coastal goods and vessels carrying coastal goods. These provisions do not apply to baggage and stores (Section 91).

The important provisions relating to coastal goods and vessels carrying coastal goods are given below:

(a) Entry of Coastal Goods

The consignor of any coastal goods shall make an entry thereof by presenting to the proper officer a Bill of Coastal Goods in the prescribed form. [Section 92(1)]. The Bill of Coastal Goods (Form) Regulations, 1976 have prescribed the Form for purposes of this Section.

Every such consignor while presenting a bill of coastal goods shall, at the foot thereof, make and subscribe to a declaration as to the truth of the contents of such bill.

(b) Coastal Goods not to be Loaded until Bill relating thereto is passed

Section 93 lays down that the master of a vessel shall not permit the loading of any Coastal goods on the vessel until a bill relating to such goods presented under Section 92 has been passed by the proper officer and has been delivered to the master by the consignor.

(c) Clearance of Coastal Goods at Destination

Section 94 lays down that the master of a vessel carrying any coastal goods shall carry on board the vessel all bills relating to such goods delivered to him under Section 93 and shall immediately on arrival of the vessel at any customs or coastal port, deliver to the proper officer of the port all bills relating to the goods which are to be unloaded at the port. Section 94(1) provides that where any coastal goods are unloaded at any port, the proper officer shall permit clearance thereof if he is satisfied that they are entered in a bill of coastal goods delivered to him under Sub-section (1).

(d) Master of a coastal vessel to carry an advice book

Section 95 lays down that the master of every vessel carrying coastal goods shall be supplied with a book to be called the advice book. The proper officer at each port of call by such vessel shall make such entries in the advice book as he deems

fit, relating to the goods loaded on the vessel at that port. The master of every such vessel shall carry the advice book on board the vessel and shall on arrival at each port of call, deliver it to the proper officer at that port for his inspection.

(e) Loading and Unloading of Coastal Goods at Customs Port or Coastal Port Only

As per Section 96, no coastal goods shall be loaded on, or unloaded from any vessel at any port other than a customs port or a coastal port appointed under Section 7 for the loading of such goods.

(f) No Coastal Vessel to Leave Without Written Order

Section 97 provides that, the master of a vessel which has brought or loaded any coastal goods at a customs port shall not cause or permit the vessel to depart from such port until a written order to that effect has been given by the proper officer.

No such order shall be given until:

- (a) the master of the vessel has answered the question put to him under Section 38;
- (b) all charges and penalties due in respect of that vessel or from the master thereof have been paid or the payment secured by such guarantee or deposit such amount as the proper officer may direct.
- (c) the master of the vessel has satisfied the proper officer that no penalty is leviable on him under Section 116 or the payment of any penalty that may be levied upon him under that section has been secured by such guarantee or deposit of such amount as the proper officer may direct.
- (d) the provisions of this Chapter and any rules and regulations relating to coastal goods and vessels carrying coastal goods have been complied with. [Section 97(2)].

(g) Application of certain provisions of this Act to coastal goods, etc.

Section 98 provides that Sections 33, 34, 36 shall, so far as may be apply to coastal goods as they apply to imported goods. Sections 37 and 38 shall, so far as may be, apply to vessels carrying coastal goods as they apply to vessels carrying imported goods or export goods.

The Central Government may by notification in the Official Gazette, direct that all or any of the other provisions of Chapter V and provisions of Section 45 shall apply to coastal goods subject to such exceptions and modifications as may be specified in the notification.

(h) Vessels carrying coastal goods exclusively — Relaxation in Customs procedures

In exercise of the powers conferred by Section 98A of the Customs Act, 1962 (52 of 1962), the Central Government has exempted vessels carrying exclusively coastal goods from the provisions of Section 92, Section 93, Section 94, Section 97 and Sub-section (1) of the Section 98 of the said Act, vide Notification No. 43/97-Cus. (N.T.), dated 11.9.1997.

The relaxations are applicable to the vessels which exclusively carry coastal goods and ply as coastal vessels. It will not be applicable for vessels which convert the status from foreign run to coastal run and vice versa. The loading and unloading operation by coastal vessels must take place at separate and exclusive berths in the ports where both coastal and foreign traffic is handled. The provisions of Sections 95, 96 and 98(2) will also remain operative in case of such vessels. In terms of Section 95, the master of vessels is required to maintain "advice book" and the proper officer of customs can inspect the book and make entries as he deems fit, relating to goods loaded at the port.

In terms of Section 96 the coastal goods can only be loaded or unloaded at places notified under Section 7 of the Customs Act, 1962. In terms of Section 98(2), the provisions contained in Sections 37 and 38 are applicable for coastal goods as applicable to vessels carrying import and export goods.

Accordingly, the Customs Officers would continue to have powers to board any vessels carrying coastal goods and can require the person incharge of vessels to produce any documents and to answer any question. They should devise selective checks of coastal vessels, at random both at the ports of loading and unloading so that there is effective check and the impression that the department has abdicated its responsibility, does not gain ground.

The light dues charges leviable on such coastal vessels may be collected by the customs till alternate arrangements are made by Ministry of Surface Transport.

In case of the vessels which change their status from foreign to coastal or vice versa, the existing provisions contained under Chapter XII of the Customs Act, 1962 shall continue to be operative. [C.B.E. & C. Circular No. 40/97-Cus., dated 19.9.1997].

(i) Power to make rules in respect of coastal goods and coastal vessels

Section 99 empowers the Central Government to make rules for:

- (a) Preventing the taking out of India of any coastal goods the export of which is dutiable or prohibited under this Act or any other law for the time being in force.
- (b) Preventing in the case of a vessel carrying coastal goods as well as imported or export goods, the substitution of imported or export goods by coastal goods.

(j) Customs duty collection of ship stores consumed during coastal run

The procedure relating to recovery of duty on ship stores consumed by foreign going vessels during their temporary reversion into coastal run has been reviewed by the C.B.E. & C. In modification of existing procedure, it has been decided that if the Steamer Agents do not desire to pay duty on the entire quantity of Bonded stores carried by the ship, it is open to them to take the estimated quantity out of the Bonded stores and pay duty on the same. The remaining quantity may remain on board such vessels in terms of Section 86 of the Customs Act, 1962. The duty on stores like alcoholic liquor, cigarettes, etc. (other than liquid cargo like, diesel, furnace oil etc.) may be recovered on quantity likely to be consumed during coastal

run, and remaining quantity may be kept in bond under custom seal as per procedure laid down under Imported Stores (Retention on Board) Regulations, 1963. The Steamer Agents are required to file the Bill of Entry as soon as the conversion takes places, and the assessment would be completed and duty collected within 7 days of the date of conversion to coastal run.

The duty on bunkers like, diesel furnace oil etc. may be recovered at 110% (One hundred and ten) of the duty leviable on the quantity estimated to be consumed during the coastal run at the time of conversion from foreign run to coastal run on provisional assessment basis. The steamer agent may file refund claim if any to get refund of duty at the time of conversion from coastal to foreign run. The assessment may be finalised within 15 days of reconversion from coastal to foreign run.

(k) Vessels carrying coastal goods exclusively—Relaxation in Customs procedures

1. In continuation of earlier measures, on the above subject the following further measures have also been taken by the Board regarding relaxation in Customs procedures in case of vessels carrying coastal goods exclusively.
2. By Notification No. 14/98-Cus. (N.T.), dated 27.2.1998, the earlier Notification No. 52-Cus., dated 1.2.1963 has been rescinded. The earlier Notification No- 52-Cus., dated 1.2.1963 required the vessels carrying coastal goods to file IGM/EGM in terms of the provisions contained in Sections 30 and 41 of the Customs Act, 1962. Consequently the vessels carrying exclusively coastal goods will not be required to file IGM/EGM.
3. In terms of Notification No. 15/98-Cus. (N.T.), dated 27.2.1998, vessels carrying exclusively coastal goods have been exempted from the delivery of Advice Book on arrival at each port of call to the proper officer of Customs at that port, as required under Sections 95(1) and 95(2) of Customs Act, 1962. However, the master of each vessel shall carry the Advice Book on Board the vessel, and the proper officer of Customs may, whenever he deems necessary, call for the Advice Book for his inspection or inspect the same of board the vessel. [M.F.(D.R.) Circular No. 16/98-Cus., dated 11.3.1998].

7.29 Duty Drawback

The term 'drawback' is applied to a certain amount of duties of Customs and Excise, sometimes the whole, sometimes only a part, remitted or paid back by Government on the exportation of the commodities on which they were levied. To entitle goods to drawback, they must be exported to a foreign port, the object of the relief afforded by drawback being, to enable the goods to be disposed of in a foreign market as if they had been never taxed on account of duties of Customs and Excise (and thus at prices save the added burden of these taxes).

For Customs purposes, drawback means, the refund of duty of Customs and duty of Central Excise that are chargeable on imported and indigenous materials used in the manufacture of exported goods. Drawback, as the name itself suggests is procedure to relieve export goods of duties borne by them at various stages of their manufacture.

7.29.1 Statutory Provisions in the Customs Act, 1962

The provisions relating to drawback are enumerated in Chapter X, in Sections 74, 75, 75A and 76, of the Customs Act, 1962. Drawback is allowed subject to conditions mentioned in Sections 74 to 76 and notifications issued thereunder, in respect of duty paid on:

- (a) imported goods, which are re-exported as such (without use),
- (b) imported goods, which are re-exported after use,
- (c) imported material used in the manufacture of goods exported.

7.29.2 Section 74 of Customs Act, 1962 — Drawback allowable on re-export of duty (Customs Import Duty) paid goods

The elements necessary to consider a claim for Drawback under Section 74 Customs Act, 1962 are:

- (i) The goods on which the drawback is claimed must have been previously imported;
- (ii) Import duty must have been paid on these goods when they were imported;
- (iii) The goods must be entered for re-export within two years from the date of payment of duty. However, it is provided that in any particular case this period of two years may, on sufficient cause being shown, be extended by the Board by such further period it may deem fit;
- (iv) The goods are identified to the satisfaction of the Assistant Commissioner of Customs as the goods that were imported;
- (v) The goods must be actually re-exported to any place out-side India;
- (vi) The goods must be capable of easy identification; and
- (vii) The market price of such goods must not be less than the amount of drawback claimed.

The Central Government has been empowered to make rules for the purpose of carrying out the provisions of Section 74 and, in particular, such rules may:

- (a) provide for the manner in which the identity of goods imported in different consignments which are ordinarily stored together in bulk, may be established;
- (b) specify the goods which shall be deemed to be not capable of being easily identified; and
- (c) provide for the manner and the time within which a claim for payment of drawback is to be filed.”

In exercise of the powers conferred under the amended Rule 74 [under clause (c) of Sub-section (3) of Section 74, above], the Central Government has framed the Re-export of Imported Goods (Drawback of Customs Duties) Rules, 1995. These rules have been issued specifying the procedure for filing a claim in respect of goods exported under a claim for drawback under Section 74 as it had become necessary to prescribe a procedure for filing of a claim in view of Section 75A of the Customs Act which now requires the Government to pay interest at the specified rates in case drawback is not paid to the exporter within one month from the filing of his claim.

(a) Rates of Drawback of Import Duty Admissible under Section 74

Two types of cases are covered in the above category. They are:

- (i) Imported goods exported as such, without putting into use — the drawback given is 98% of duty paid on import. (The idea behind withholding 2% is to cover administrative expenses).
- (ii) Imported goods exported after use.

If the goods had been used after import and then exported the rate of drawback i.e. the percentage of duty refunded will be according to the period of usage, between the date of clearance for home consumption and the date when the goods are "placed under Customs Control" for exports. The rate of drawback in this case is not fixed and progressively decreases as the period of use increases as enumerated in Customs Notification No. 19 dated 6.2.1965 as amended by Customs Notification No. 45/70 dated 2.5.1970. In satisfying the condition "placed under Customs Control", it is necessary that the "Shipping Bill" should be filed and the goods "physically brought in to Customs area" for export and placed under the control of Customs.

Customs Notification No. 19 dated 6.2.1965 (as amended) while setting out the rates of drawback, differentiates as between two categories of goods, in the grant of drawback:

- (a) Goods imported by a person for his personal and private use and motor cars; and
- (b) Other goods.

For the category (a) above, the goods imported by a person for his personal and private use, may be exported as "baggage" and he shall make a declaration, (Baggage declaration - the format used for clearance of unaccompanied baggage) which declaration shall be deemed to be an "Entry for Export".

The drawback rates are calculated in regard to the above (a) category of goods, by reducing the Import duty paid by 4%, 3%, 2-1/2% and 2% for use, for each quarter or part thereof during the period of First, Second, Third and Forth year respectively.

Even though the rates are provided as above, in the notification, for grant of drawback for goods imported for personal and private use, and used for more than 2 years, the Commissioner of Customs could grant extension of time limit (beyond two years) but no drawback is admissible beyond 4 years.

On the category of goods covered by (b) above, the percentage of import duty payable as drawback depends on the period of usage of such goods as detailed below:

(b) Rate fixed by Government under Section 74(2) by Notification No. 23/2008-Cus., dt. 1.3.2008.

Period of use	D.B. Rate
Not more than 3 months	95%
3-6 months	85%
6-9 months	75%
9-12 months	70%

12-15 months	65%
15-18 months	60%
Above 18 months	NIL

For Motor Vehicles

Use per quarter during	Percentage of Reduction
1st Year	4%
2nd Year	3%
3rd Year	2.5%
4th Year	2%

For use over 24 months extension of time-limit by the Commissioner is required before grant of drawback. Also drawback shall not be given on the following goods if used after their importation:

- (i) Wearing apparel.
- (ii) Tea-chests.
- (iii) Exposed cinematograph films passed by the Board of Film Censors in India.
- (iv) Unexposed photographic films, paper and plates and X-ray films.

(c) Drawback under Section 75 of the Customs Act, 1962—Drawback on Imported Materials used in the Manufacture, Processing or Operation of Goods which are Exported

As distinct from Section 74 of the Customs Act, 1962, Section 75 postulates repayment of a part or whole of the duty paid on materials imported and used in manufacturing of goods which are exported as manufactured items outside India. Section 75 has been amended by the Finance Act, 1995 to permit drawback not only on materials/inputs used in the manufacture but also processed or subjected to any other operation for export of goods from India. The amendment is made to overcome the difficulty caused by the restricted meaning of the word “manufacture” in Section 75(1) of the Customs Act.

Drawback, as the name itself suggests, particularly with reference to Section 75 of the Customs Act, 1962, is a procedure to relieve the export goods of duties borne by goods at various stages of their manufacture, processing or any other operation carrying out on them. Such relief is allowed in respect of duties paid on raw-materials, and components utilised in the manufacture, processing etc. of goods. The wastages involved in the manufacture, processing etc. and the duty incidence(s) on the packing materials used in the Export of the goods are also taken into account. Drawback is allowed not only on duties incurred in the “Direct Imports” of materials or components utilised in the manufacture, processing etc. of Export goods but also on earlier inputs that go into the raw-materials and manufacture, processing etc. of components. Therefore, the rates of drawback are fixed by the Government on “average basis”, on the basis of the relevant data obtained from the leading manufacturers or the persons carrying out any process or any other operation either for a class of goods or for specific goods. The procedure set out in Section 75 of Customs Act, 1962, as reproduced hereunder, the Customs and Central Excise Duties Drawback Rules, 1995 allow of drawback, of Customs duties and Central Excise duties that are chargeable on imported and indigenous materials respectively,

used in the manufacture, processing or any other operation carried out on goods exported under claim for Drawback.

(d) Section 75 of the Customs Act, 1962 — Drawback on imported materials used in the manufacture of goods which are exported

- (1) Where it appears to the Central Government that in respect of goods of any class or description manufactured, processed or on which any operation has been carried out in India, being goods which have been entered for export and in respect of which an order permitting the clearance and loading thereof for exportation has been made under Section 51 by the proper officer, or being goods entered for export by post under Section 82 and in respect of which an order permitting clearance for exportation has been made by the proper officer, a drawback should be allowed of duties of customs chargeable under this Act on any imported materials of a class or description used in the manufacture or processing of such goods or carrying out any operation on such goods, the Central Government may, by notification in the Official Gazette, direct that drawback shall be allowed in respect of such goods in accordance with and subject to the rules made under Sub-section (2).

Provided that no drawback shall be allowed under this sub-section in respect of any of the aforesaid goods which the Central Government may, by rules made under Sub-section (2), specify, if the export value of such goods or class of goods is less than the value of the imported materials used in the manufacture or processing of such goods or carrying out any operation on such goods or class of goods, or is not more than such percentage of the value of the imported materials used in the manufacture or processing of such goods or carrying out any operation on such goods or class of goods as the Central Government may, by notification in the Official Gazette, specify in this behalf:

Provided further that where any drawback has been allowed on any goods under this sub-section and the sale proceeds in respect of such goods are not received by or on behalf of the exporter in India within the time allowed under the Foreign Exchange Management Act 1999, such drawback shall except under such circumstances as the central government may, by rules, specify be deemed never to have been allowed and the Central Government may, by rules made under Sub-section (2), specify the procedure for the recovery or adjustment of the amount of such drawback.

- (1A) Where it appears to the Central Government that the quantity of a particular material imported into India is more than the total quantity of like material that has been used in the goods manufactured processed, or on which any operation has been carried out in India and exported outside India, then, the Central Government may, by notification in the Official Gazette, declare that so much of the material as is contained in goods exported shall, for the purpose of Sub-section (1), be deemed to be imported material.
- (2) The Central Government may make rules for the purpose of carrying out the provisions of Sub-section (1) and, in particular, such rules may provide:
- (a) for the payment of drawback equal to the amount of duty actually paid on the imported materials used in the manufacture or processing of the

goods or carrying out any operations on the goods or as is specified in the rules as the average amount of duty paid on the materials of that class or description used in the manufacture or processing of export goods or carrying out any operation on export goods of that class or description either by manufacturers generally or by persons processing or carrying on any operation generally or by any particular manufacturer or particular person carrying on any process or other operation and interest if any, payable thereon;

- (aa) for specifying the goods in respect of which no drawback shall be allowed;
- (ab) for specifying the procedure for recovery or adjustment of the amount of any drawback which had been allowed under Sub-section (1) or interest chargeable thereon.
- (b) for the production of such certificates, documents and other evidence in support of each claim of drawback, as may be necessary;
- (c) for requiring the manufacturer or the person carrying on any process or any other operation to give access to every part of his manufactory to any officer of customs specially authorised in this behalf by the Assistant Commissioner of Customs to enable such authorised officer to inspect the process of Manufacture, process or any other operations carried out and to verify by actual check or otherwise the statements made in support of the claim for drawback.
- (d) for the manner and the time within which claim for payment of drawback may be filed;
- (3) The power to make rules conferred by Sub-section (2) shall include the power to give drawback with retrospective effect from a date not earlier than the date of changes in the rates of duty on inputs used in export goods.

(e) Payment of Interest on Drawback

Section 75A of the Customs Act provide for levy of interest on delayed payment of drawback. Interest at such rate as may be fixed by the Board would be allowed in case payment against a claim for drawback is not made within one* month of filing the claim in the prescribed manner. Likewise, when a drawback claim has been allowed erroneously, interest at the prescribed rate would be payable if the excess amount is not deposited with the Government within one* month of the amount being demanded.

Section 75A reads thus:

- 75A (1) Where any drawback payable to a claimant under Section 74 or Section 75 is not paid within a period of *one month from the date of filing a claim for payment of such drawback, there shall be paid to that claimant in addition to the amount of drawback, interest at the rate fixed under Section 27A from the date after the expiry of the said period of *one month till the date of payment of such drawback.

* Substituted for the words, "two months" by the Financial Act, 2003.

- (2) Where any drawback has been paid erroneously or it becomes otherwise recoverable under the Act or the rules made thereunder, the claimant shall, within a period of two months from the date of demand, pay interest. The amount of interest shall be calculated from the date of payment of such drawback to the claimant till the date of recovery of such drawback. [Section 75A(2)].

(f) Prohibition and Regulation of drawback in certain cases — Section 76 of the Customs Act

Independent of other conditions which are laid down in Sections 74 and 75 of Customs Act, 1962 and in the Drawback Rules, no drawback will be granted:

- (a) in respect of any goods the market price of which is less than the amount of drawback due thereon; and
- (b) where drawback due on any goods is less than ₹ 50.

Also, if the Central Government is of opinion that specified goods on which drawback is claimed are likely to be smuggled back into India, it may stipulate that drawback be paid subject to certain conditions. There are three notifications in this regard:

Notification 50/63 dt. 1.2.63 as amended by 153/68 dt. 29.10.68 lays down that goods if exported on vessels less than 1,000 tons are likely to be smuggled back into India than export under claim for drawback may be permitted on the following conditions:

- (i) The agent of the vessel executes a bond in a sum equal to the amount of drawback and in such form and manner as the proper officer deems fit. The terms of the bond shall be that if the agent of the vessel produces to the proper officer, within three months or within such extended period as the proper officer may allow, a certificate issued by the Customs authorities at the port of destination that the goods have been landed at the port the bond shall stand discharged; but otherwise a sum equal to the amount of drawback allowed on the goods in respect of which the said certificate is not produced shall stand forfeited. The above bond shall be with such surety or security or both as is required by the Customs.
- (ii) The exporter produces to the proper officer a certificate issued by the Customs Authorities at the port of destination that the goods have been landed at the port or a certificate from the authorised dealer.

Under Notification 51/1.2.63 the following goods put on board a vessel less than 200 tons for use as stores are not to be given drawback:

- (i) alcoholic liquors;*
- (ii) cigarettes;*
- (iii) cigars;*
- (iv) pipe tobacco.*

Notification 208/1.10.77 lays down that drawback is not to be allowed on exports

to Bhutan, Nepal or by land to Burma, Tibet or Sinkiang except on certain conditions given in the said Notification.

(g) Duty Drawback Rates under Section 75 (Drawback Rules)

The duty drawback scheme is presently administered by the Directorate of Drawback in the Ministry of Finance. Drawback on exports is sanctioned and paid by the concerned Commissioner of Customs or Central Excise incharge of the port/airport/Land Customs Station through which the goods are exported, at the rates determined by the Directorate. These drawback rates are fixed either for a class of products manufactured in the country which are available to all exporters, and known as All-industry Rates or for a product of a particular manufacturer — known as Brand Rate. The rates are reviewed and revised periodically taking due note of variation in consumption pattern of inputs and duties suffered thereon. The Drawback is admissible irrespective of mode of export i.e. whether despatched by Sea, Air, Land Customs Station or Parcel Post.

Pursuant to the amendments made in sections dealing with drawback in the Customs Act and to streamline the existing rules, it was considered necessary to revise the Customs and Excise Duties Drawback Rules, 1971. Accordingly, Customs and Central Excise Duties Drawback Rules, 1995 were issued in supersession of 1971 Rules.

(h) Procedure for Fixation of All-industry Rates

Under Rule 3 of the Drawback Rules, the Central Government determines the rate(s) of drawback in respect of certain classes of goods and notifies the same through public notices. Any exporter of these goods can claim Drawback at All Industry Rates. He is, however unless otherwise specifically provided, debarred from availing these rates as per General Notes laid down in the relevant Public Notice issued annually if he has been otherwise permitted certain concessions e.g. facility of manufacture in Bond, duty free imports under Advance Licensing/Import-Export Pass Book Scheme, facility of exports under Central Excise Rules, etc. (In such cases, for any unrebated customs or central excise duties, facility of Brand Rates is generally provided).

All Industry rates are reviewed by the Government annually, taking due note of Budgetary changes and revised wherever necessary, taking into account the changes in the duty incidence consequent to changes in the rate of Customs or Central Excise Duties and or the variations in the prices of various inputs (where the rates of duties are ad valorem). The revised All Industry Rates are generally made effective from 1st June and are normally kept unchanged for 1 year. If changes in duties on basic inputs of a product at any point of time (after the presentation of Budget) are substantial, the corresponding All industry Rates are reviewed and appropriate change is also effected in between the year. From time to time new products are also added to the list of goods having All Industry Rates.

In determining the All Industry Rates, for a particular class of goods, as per Rule 3(2) of Drawback Rules, the Central Government takes into account the following:

- (i) the average quantity or value of each class or description of the materials

from which a particular class of goods are ordinarily produced or manufactured in India;

- (ii) the average quantity or value of the Imported material or excisable materials used for production or manufacture in India;
- (iii) the average amount of duties paid on Imported materials or excisable materials used in the manufacture of the semis, components and intermediate products used in the manufacture;
- (iv) the average amount of duties paid on materials wasted in the manufacturing process and catalytic agents (If such waste or catalytic agent is re-used in any process of manufacture or sold, the average amount of the duties on the waste or catalytic agent re-used/sold shall be deducted);
- (v) the average amount of duties paid on imported materials or excisable materials used for containing or packing the export product; and
- (vi) any other information considered relevant for determining the drawback rate.

(i) Brand Rates

Where the Central Government has not determined the All Industry rates of drawback in respect of any export product eligible for such drawback (set out in Schedule to the Drawback Rules), or where the rate is not eligible because the manufacturer of the product has availed of certain duty free facilities (like Advance Licence/Import-Export Pass Book etc.) but where sufficient duty paid inputs are also used, any manufacturer or exporter of such goods may apply under Rule 6 of the Drawback rules to the Central Government for the determination of the drawback rate for his product of specified description/characteristics.

(j) Special Brand Rates

In case any manufacturer/exporter finds that the All industry rate of drawback for any class of goods is less than four-fifth of the duties paid on the materials or components used in the production/manufacture and packing of same goods being exported by him, he can make an application for fixation of an appropriate amount or rate of drawback (under Rule 7 of the Drawback Rules) for his products of specified description/characteristics. Such rates, wherever determined, are termed as 'Special Brand Rates'.

(k) Provisional Rate of Drawback

Exporters have also the facility to apply for fixation of a provisional drawback rate as per provisions of Rule 6(2)(a) of Drawback Rules, in cases where they have already applied for fixation of brand rates/special brand rates of their products whose finalisation is pending. The payment at provisional rates is, however, subject to execution of a suitable bond (with surety/security) by the Exporter with the concerned Custom House. On finalisation of the rate, the differential amount is appropriately adjusted.

(l) Minimum Rate of Drawback

As per Rule 8 of the Drawback Rules, for any export product where the duties

paid on inputs work out to less than 1% of F.O.B. value thereof (except where the amount of drawback per shipment exceeds rupees Five hundred), no Drawback rate (All-industry Rate or Brand Rate) is determined. However, this condition of minimum 1% of F.O.B. value will not be applicable in case exports are made by post and exports are made in discharge of obligation against Advance Licences issued under Duty Exemption Scheme. Thus, in case of exports made by post and exports under Duty Exemption Scheme, drawback shall be payable in all cases wherever the amount of drawback is more than ₹ 50/-, the minimum limit specified statutorily in Section 76 of the Customs Act.

Further, under sub-rule (2), of Rule 8 it is provided that no amount or rate of drawback shall be determined in respect of any goods or class of goods under Rule 6 or Rule 7, as the case may be, if the export value of each of such goods or class of goods in the bill of export or shipping bill is less than the value of the imported materials used in the manufacture of such goods or class of goods, or is not more than such percentage of the value of the imported materials used in the manufacture of such goods or class of goods as Central Government may, by notification in the Official Gazette, specify in this behalf.

An 'Explanation' added to Sub-rule (2) provides that "Export Value" in relation to any export goods means the value thereof, determined in accordance with the provisions of Sub-section (1) of Section 14 of the Customs Act, 1962.

For full text of Customs and Central Excise Duties Drawback Rules, 1995, students may refer to the latest Customs Law Manual.

In *U.O.I. v. Rajindra Dyeing and Printing Mills*, 2005 (180) ELT 433 (SC) it was held that export is complete when goods cross territorial waters of India. If ship sinks within territorial waters, export is not complete and DDBK not payable.

7.30 Transportation of Goods

(a) Transit and Transshipment of Goods

Concept: A conveyance / vessel may reach a port but may not unload the goods at that port. It may halt at the port for any other purpose such as repairs, replenishment of supplies, refueling etc. Once the purpose is over, it may start sailing to the destination port. In this case two ports are involved. Halting port (known as transit port) intermediate port and destination port (called as port of clearance). Such a phenomenon of temporary stay at a port other than a destination port is called transit goods. In transit goods same vessel reaches the port of clearance.

In transshipment, the vessel reaching an intermediate port, transfers the goods to another vessel and the second vessel into which the goods are transferred (loaded) from the 1st vessel, carries the goods to the destination port. E.g. a ship A comes to Mumbai from South Africa and some goods are transshipped (transferred) to some other ship B and the goods are meant to be delivered at Cochin port (destination port) A goes back to South Africa after delivery at Mumbai port and the B reaches Cochin, transshipment took place at Mumbai port.

In brief, in case of transit goods, same vessel reaches the port of clearance after some halt at an intermediate port, but in transshipment some other vessel carries the goods to the destination port. Thus, in transshipment, at least two vessels are

involved. And in the case of both transit and transshipment, the destination port may be Indian Port or Foreign port but the transit/transshipment port is necessarily Indian.

Customs Act, 1962 contains separate provisions for goods in transit in Chapter VIII of the Act. This Chapter consists of Sections 52 to 56. Section 52 of the Act makes it very clear that the provisions of Chapter VIII do not apply to:

- (a) baggage;
- (b) goods imported by post;
- (c) stores.

Sections 53, 54 and 55 have been amended by the Finance (No. 2) Act, 1998, so as to also allow for the transit and transshipment of goods in the following circumstances:

- (a) where goods have arrived in India at a land customs station and are intended to be transhipped to another land customs station or to a port or airport outside India;
- (b) where goods have been carried in a conveyance other than a vessel or aircraft; and
- (c) where goods that have arrived at the port or airport on a vessel or aircraft are required to be transhipped to a land customs station.

The details of the provisions of the Chapter are discussed hereinbelow:

(b) Transit of certain goods without payment of duty

Section 53 of the Act deals with this. Accordingly, any goods imported in a conveyance and mentioned in the import manifest or the import report, as the case may be, as for transit in the conveyance to any place outside India or any Customs station may be allowed to be so transited without payment of duty. The provisions of Section 53 are subject to the provisions of Section 11. It should be noted that Section 53 talks about transit of goods in the same conveyance and not transshipment of goods from one conveyance to another. (Section 54 deals with transshipment of goods imported into India, from one land customs station to another land customs station or to a port or airport outside India).

(c) Transshipment of certain goods without payment of duty

Section 54 of the Act provides that where any goods imported into a Customs station are intended for transshipment, a bill of transshipment shall be presented to the proper officer in the prescribed form. But where the goods are being transhipped under an international treaty or bilateral agreement between the Government of India and Government of a foreign country, a declaration for transshipment instead of a bill of transshipment shall be presented to the proper officer in the prescribed form.

Sub-section (2) of Section 54 provides that where any goods imported into a Customs station are mentioned in the Import Manifest or import report as the case may be, as for transshipment to any place outside India, such goods may be allowed to be so transhipped without payment of duty. The provisions of Sub-section (2) of Section 54 are subject to the provisions of Section 11.

Sub-section (3) of Section 54 provides that where any goods imported into a Customs station are mentioned in the Import Manifest or import report, as the case may be, as for transhipment:

- (a) to any major port as defined in the Indian Ports Act, 1908 or the Customs Airport at Mumbai, Calcutta, Delhi or Chennai or any other Customs port or Customs airport which the Board may, by Notification in the Official Gazette, specify in this behalf, or
- (b) to any other Customs station and the proper officer is satisfied that the goods are bona fide intended for transhipment to such Customs station,

the proper officer may allow the goods to be transhipped without payment of duty subject to such conditions as may be prescribed for the due arrival of such goods at the Customs station to which transhipment is allowed.

(d) Liability of duty on goods transited under Section 53 or transhipped under Section 54

Under Section 55 of the Act, where any goods are allowed to be transited or transhipped under Sections 53 and 54 respectively, to any Customs station, they shall, on their arrival at such station, be liable to duty and shall be entered in like manner as goods are entered on the first importation thereof and the provisions of this Act and any rules shall so far as may be, apply in relation to such goods.

(e) Transport of certain classes of goods subject to prescribed conditions

Sometimes imported goods may be transported from one part of the country to another part of the country through a foreign territory because of geographical and other constraints. Under the circumstances, Section 56 provides that imported goods may be transported without payment of duty through any foreign territory subject to the Transportation of Goods (Through Foreign Territory) Regulations, 1965. These regulations contemplate the following procedure. Regulations 3 and 10 of these Regulations are extracted hereinbelow:

1. Consignor to deliver a Bill:

- (a) Whenever any goods to which these regulations apply are to be transported, the consignor of the goods shall make entry to that effect by presenting to the proper officer a bill (in duplicate) in the form specified in Appendix C to these Regulations.
- (b) Every such consignor shall, while presenting the bill, make and subscribe to a declaration at the foot thereof as to the truth of its contents.

2. Permission to load goods, etc.: No person-in-charge of a vessel shall permit the loading of such goods on a conveyance unless:

- (a) the bill relating to them after approval by, and
- (b) a written permission to load the goods from, proper officer are received by him.

3. Execution of Bond: Before any such goods are permitted to be loaded on the conveyance, the consignor or the person-in-charge of the vessel shall

be required to execute a bond in such form and with such surety or sufficient security as the proper officer may demand, binding himself in an amount not exceeding the value of the goods.

4. Duties of the person-in-charge of the conveyance:

- (1) On receipt of the documents referred to in regulation 4, the person-in-charge of the conveyance shall prepare as many sets of Manifest (in triplicate) in the Form specified in Appendix B to these regulations in respect of such goods as there are customs stations to be passed through on the route.

He shall, immediately, on arrival at an customs station of delivery or re-entry, deliver a set of the manifest along with the bill or bills relating to the goods to the proper officer at the customs station.

- (2) The proper officer shall, after making the necessary checks, make an endorsement on the manifest, retain one copy of the manifest and return the other two copies to the person-in-charge of the conveyance.
 - (3) The person-in-charge of the conveyance shall retain one of the two copies for carrier's record and present the other to the proper officer at the loading station.
 - (4) The person-in-charge of the conveyance carrying such goods shall not leave the customs station until a written permission has been given by the proper officer after checking the manifest presented to him under the regulation.
- 5. Delivery of bills at the destination station:** The person-in-charge of the conveyance shall carry with him on the journey all the bills relating to the goods delivered to him and shall immediately on arrival at any customs station. deliver to the proper officer such of the bills as relate to the goods unloaded at that station.
- 6. Clearance of goods:** Such goods, after being unloaded at any customs station, shall not be cleared unless the proper officer gives a written permission that all the goods so unloaded are entered in the bill or bills delivered to him under these Regulations.
- 7. Terms of the bond:** The condition of the bond to be executed under Regulation 5 shall be that if the person-in-charge of the conveyance or the consignor produces proof within a time stipulated in the bond or such extended time as the proper officer may permit that the goods have been produced before the proper officer at destination the bond shall be void; and if such proof be not furnished the executor of the instrument shall be liable to pay an amount equal to the export duty leviable on the goods and such penalty as may be adjudged or imposed by the proper officer under the Customs Act, 1962, the Imports and Exports (Control) Act, 1947 (18 of 1947) or the Foreign Exchange Management Act, 1999 and shall also be liable to forfeit the whole amount of the bond.
- 8. Execution of general bond:** Notwithstanding anything contained in these Regulations, the proper officer may permit the person-in-charge of the conveyance or the consignor of goods to enter into a general bond in such

form and with such surety or security as the proper officer may deem fit, in respect of transport of goods as above said to be effected from time to time”.

7.31 Warehousing

Introduction

Goods imported from abroad may be cleared straightaway by the Importers by filing the Customs Clearance document, the Bill of Entry for Home Consumption (White Bill of Entry) alongwith all the documents, such as Invoice, Purchase Contract, Import Licence (Wherever necessary) and all connected and relevant documents. The above requirements for clearance are stipulated in Section 46 of the Customs Act, 1962.

Section 46 of the Customs Act, 1962 also provides for the Importer filing a Bill of Entry, either for Home consumption or for Warehousing, in the “prescribed form”. Therefore, the importers who do not intend clearing the imported goods for “Home consumption” straightaway, may choose to “warehouse” the goods (store the goods under Customs control/custody) and clear the same subsequently either wholly or in part, in piecemeal, on payment of Customs duty.

Warehousing is a very useful facility in export import business. Importer can deposit the dutiable goods in a bonded warehouse without payment of duty. This facility is available to traders as well as importers.

Warehousing facility is availed for the following reasons:

- (i) The importer may not require the goods immediately.*
- (ii) He may intend to clear the goods under advance license scheme without payment of import duty if license is not on hand at the time of import then he can deposit first and submit the license at the time of clearance.*
- (iii) The importer may not have enough funds to make payment of duty immediately.*
- (iv) He intends to re-export the imported goods after some process/ repacking, repairing etc.*
- (v) He wants to avoid heavy demurrage charges imposed by the port.*
- (vi) Any other reason the importer feels it convenient.*

In terms of Sub-sections (1) to (4) of Section 17 of the Customs Act, 1962, after an Importer had “entered” any imported goods under Section 46 *ibid* (after an importer had presented the Bill of Entry), they are examined and tested if so warranted and assessed to Customs duty. The prescribed form’ referred to in Section 46 of the Customs Act 1962 also includes the Bill of Entry for warehousing. This form is also referred to and understood by the following names:

- (a) “Into Bond” Bill of Entry;
- (b) “Yellow” Bill of Entry;

- (c) "Warehousing" Bill of Entry; and
- (d) "Buff" Bill of Entry.

The term "warehouse" for the purposes of the application of the provisions of the Customs Act, 1962 has been defined under Section 2(43) of the Act, as under:

"Warehouse" means a Public (Bonded) warehouse appointed under Section 57 of the Customs Act or a private (Bonded) warehouse "Licensed" under Section 58 of Customs Act, 1962.

Warehouses either "public" or "private", could be "appointed" or "licensed" as above said, only at the places declared by the Central Board of Excise and Customs to be "warehousing stations" by means of notifications in the official gazette. Therefore, warehouses cannot be "appointed" or "licensed" in all places. [Section 9 of the Customs Act, 1962].

In earlier years, the port towns adjacent to the major ports and contiguous areas thereto, which were easily accessible and which could be kept under control of the respective Customs "Warehouse" only was declared as "warehousing stations". For the purpose of convenience, entire cities, talukas, in such cases were generally declared as warehousing stations, generally or for specific purposes.

Consequent upon the increased requirements for adequate warehousing facility, of the trade and industry, now the Government of India's policy in respect of Public (Bonded) warehousing, is to declare selected places, in the areas other than port areas, namely in Inland/Interior areas, as "warehousing stations" under Section 9 of the Customs Act, 1962.

The object behind "appointment of Public (Bonded) warehouses and licensing of Private (Bonded) warehouses" is to afford a facility to the Importers to deposit the imported goods for the specified period, before they are cleared for home consumption or re-export.

Chapter IX (Sections 57 to 73) deals with various provisions relating to warehousing of import goods.

These provisions may be broadly divided into the following headings:

1. Appointment of public warehouses (Section 57).
2. Licensing of Private warehouses (Section 58).
3. Warehousing bond (Section 59).
4. Permission for deposit of goods in a warehouse (Section 60).
5. Period for which goods may remain warehoused (Section 61).
6. Control over warehoused goods (Section 62).
7. Payment of rent and warehouse charges (Section 63).
8. Owner's right to deal with warehoused goods (Section 64).
9. Manufacture and other operations in relation to goods in a warehouse (Section 65).

10. Power to exempt imported materials used in the manufacture of goods in warehouse (Section 66).
11. Removal of goods from one warehouse to another (Section 67).
12. Clearance of warehoused goods for home consumption (Section 68).
13. Clearance of warehoused goods for exportation (Section 69).
14. Allowance in case of volatile goods (Section 70).
15. Procedure for taking out/removal of goods from warehouse (Sections 71 and 72).

The above provisions, as amended, are briefly explained as under:

1. *Appointing of Public Warehouses*

At any warehousing station, the Assistant or/Deputy Commissioner of Customs may appoint public warehouses wherein dutiable goods may be deposited (Section 57). Goods meant for re-export can be warehoused in these warehouses without payment of duty. The scope and functions of the scheme of appointment of public warehouses as well as the procedure to be followed are normally explained in detail through the Commissionerate's trade notices issued from time to time.

The Government of India's policy in respect of Customs Public Bonded Warehousing is mainly to provide adequate warehousing facilities at selected places in the interior keeping in view the requirement of the trade and industry, the proximity to the ports of import and the availability of Customs expertise. Such public bonded warehouse in inland area are generally managed and controlled by the Central Warehousing Corporation.

2. *Licensing of Private Warehouses*

At any warehousing station, the Assistant or/Deputy Commissioner of Customs may licence private warehouses wherein dutiable goods imported by or on behalf of the licensee or any other imported goods in respect of which facilities for deposit in a public warehouse are not available, may be deposited [Section 58(1)].

The Assistant or/Deputy Commissioner of Customs may cancel a licence granted under Sub-section (1):

- (a) by giving one month's notice in writing to licensee, or
- (b) if the licensee has contravened any provision of this Act or the rules or regulations or committed breach of any of the conditions of licence.

The licensee will, however, be given a reasonable opportunity of being heard, before any licence is cancelled under Clause (b) [Section 58(2)].

The Assistant or/Deputy Commissioner of Customs may suspend the licence, pending an enquiry whether a licence granted under Sub-section (1) should be cancelled under Clause (b) of Sub-section (2) [Section 58(3)].

The object of warehousing is to allow the facility to trade of deferring payment of duty on imported goods upto the period permissible under Section 61. However, seeing the misuse of this facility, the Customs (Amendment) Act, 1991 introduced a

new Section 59A in the Act making it obligatory to deposit 50% of the duty assessed for availing the facility and imposed several other restrictions with regard to delay in clearances. This condition of predeposit of 50% of duty has however been withdrawn by the Finance Act, 1994, w.e.f. 13.5.1994 by omission of Section 59A.

The licensing of private warehouses is permissible only at the warehousing stations notified under Section 9 of the Act. Section 58 also makes provision for circumstances when the licence given for such warehouse could be cancelled, revoked or suspended by the Assistant Commissioner of Customs.

The Government of India's policy in the case of Customs Bonded Warehousing facility at the Inland warehousing station has, hitherto, been that it should be extended only to export oriented industries. Thus, the facility of private bonded warehousing under Section 58 of the Customs Act, 1962 has been given mainly to export oriented industries and only for imported raw materials.

To provide the facility of applying for a licence for customs private bonded warehouse and for facility of storage, accounting and clearance of imported goods stored in the warehouse, detailed procedure/instructions are issued by various commissionerates from time to time.

3. Warehousing Bond

The importer of any goods specified in Sub-section (1) of Section 61, which have been entered for warehousing and assessed to duty under Section 17 or Section 18 shall execute a bond binding himself in a sum equal to twice the amount of the duty assessed on such goods:

- (a) to observe all the provisions of this Act and the rules and regulations in respect of such goods;
- (b) to pay on or before a date specified in a notice of demand:
 - (i) all duties, and interest, if any, payable under Sub-section (2) of Section 61;
 - (ii) rent and charges claimable on account of such goods under this Act, together with interest on the same from the date so specified at such rate not below eighteen per cent, and not exceeding thirty-six per cent, per annum, as is for the time being fixed by the Central Government, by notification in the Official Gazette; and.
- (c) to discharge all penalties incurred for violation of the provisions of this Act and the rules and regulations in respect of such goods [Section 59(1)].

The Assistant or Deputy Commissioner may permit an importer to enter into a general bond in such amount as the Assistant/ Deputy Commissioner of Customs may approve in respect of the warehousing of goods to be imported by him within a specified period [Section 59(2)].

A bond executed by an importer under this section in respect of any goods shall continue in force notwithstanding the transfer of the goods to any other person or the removal of the goods to another warehouse.

Where whole of the goods or any part thereof are transferred to another person,

the proper officer may accept a fresh bond from the transferee in a sum equal to twice the amount of duty assessed on the goods transferred and thereupon the bond executed by the transferor shall be enforceable only for a sum mentioned therein less the amount for which a fresh bond is accepted from the transferee [Section 59(3)].

4. Permission for Deposit of Goods in a Warehouse

When the provisions of Section 59 have been complied with in respect of any goods, the proper officer may make an order permitting the deposit of the goods in a warehouse (Section 60).

Procedure towards clearance of Imported goods for warehousing needs to be explained in brief at this stage. Section 46 of the Customs Act, requires an importer (or his agent) (Custom House Agent) to file a Bill of Entry either for Home consumption or for Warehousing. If an importer intends to deposit his consignment in a private or public (bonded) warehouse he will have to file a Bill of Entry for warehousing (yellow in colour) in quadruplicate in the Import Department of the Custom House/or in Air Cargo Complex. The Bill of Entry is "noted" in the import manifest of the respective vessel or aircraft and returned to the importer or his agent for presentation in the concerned Appraising/assessing Group in the Custom House/Air Cargo Complex. The Assessing Officer checks the quantity, value, description etc. of the goods imported and as declared in the Bill of Entry. He classifies the imported goods in accordance with the Customs Tariff and Central Excise Tariff (for countervailing duty) and indicates the classification and the rates of duties applicable to the goods. The Bill of Entry so assessed is subject to counter-check by the Group Assistant Commissioner. After counter check the amount of duty is calculated/quantified and indicated suitably on the Bill of Entry. In the above process of assessment, the assessing officer also verifies the coverage of the goods by the Import Licence produced, particularly wherever the goods are to be covered by an Import Licence validity. It is pertinent to note that the goods could be permitted to be warehoused only on their Valid Import. Thus, the Import Licence and other connected formalities are also completed.

The Bill of Entry is thereafter returned to the importer. The importer should execute a bond as required in Section 59 of the Customs Act for twice the amount of duty leviable/balance on the goods. Instead of executing bonds for each consignment imported, an importer may also furnish a general bond for a lumpsum covering twice the amount of duty leviable on goods to be imported by him during a specified period (6 months, one year, etc.).

The bond Department after completing all the required formalities including acceptance of the double duty bond, will return the warehousing Bill of Entry to the Importer/CHA after stamping the Bill of Entry with an endorsement "returned to the importer". This endorsement on all the copies of the Bill of Entry will also indicate the date on which the Bill of Entry has been returned to the Importer/CHA.

In cases where the Assessing Officer in the Group desires that the goods should be examined or tested before assessment, examination of the goods and verification of fitness for bonding are done by the Docks Air Cargo Appraising Staff. Thereafter, the Assessing Officer makes the assessment by indicating the rates of duties applicable to the goods. In such cases the "pass into bond" order is signed by the Preventive Superintendent incharge of the Bonds Department after Assistant

Commissioner (Bonds) has accepted the importer's bond for twice the amount of duty payable.

5. Period for which goods may remain warehoused

Sub-section (1) of Section 61 provides that any warehoused goods may be left in the warehouse in which they are deposited or any warehouse to which they may be removed:

- (a) in the case of capital goods intended for use in any hundred per cent export oriented undertaking, till the expiry of five years;
- *(aa) in the case of goods other capital goods intended for use in any hundred per cent export-oriented undertaking, till the expiry of three years; and
- (b) in the case of any other goods, till the expiry of one year,

after the date on which the proper officer has made an order under Section 60 permitting the deposit of the goods in a warehouse:

Explanation: For the purposes of this section, "hundred per cent export oriented undertaking" has the same meaning as in Explanation 2 to Sub-section (1) of Section 3 of the Central Excise Act, 1944 (1 of 1944).

Provided that:

- (i) in the case of any goods which are not likely to deteriorate, the period specified in Clause (a) or Clause (aa) or Clause (b) may, on Sufficient cause being shown, be extended—
 - (a) in the case of such goods intended for use in any hundred percent export-oriented undertaking by the commissioner of customs, for such period as he may deem fit; and
 - (b) in any other case, by the Commissioner of Customs, for a period not exceeding six months and by the Chief Commissioner of Customs for such further period as he may deem fit.
- (ii) in the case of any goods referred to in Clause (b), if they are likely to deteriorate, the aforesaid period of one year may be reduced by the Commissioner of Customs to such shorter period as he may deem fit.

Provided further that when the licence for any private warehouse is cancelled, the owner of any goods warehoused therein shall, within seven days from the date on which notice of such cancellation is given or within such extended period as the proper officer may allow, remove the goods from such warehouse to another warehouse or clear them for home consumption or exportation.

(2) Where any warehoused goods:

- (i) specified in sub-clause (a) or sub-clause (aa) of Sub-section (1), remain in a warehouse beyond the period specified in that sub-section by reasons of extension of the aforesaid period or otherwise, interest at such rate as is specified in Section 47 shall be payable, on the amount of duty payable at the time of clearance of the goods in accordance with the provisions of Section 15 on the warehoused goods, for the period

from the expiry of the said warehousing period till the date of payment of duty on the warehoused goods;

- (ii) specified in sub-clause (b) of Sub-section (1), remain in a warehouse beyond a period of thirty days, interest shall be payable at such rate or rates not exceeding the rate specified in Section 47, as may be fixed by the Board, on the amount of duty payable at the time of clearance of the goods in accordance with the provisions of Section 15 on the warehoused goods for the period from the expiry of the said ninety days till the date of payment of duty on the warehoused goods.

Provided that the Board may, if it considers it necessary so to do in the public interest, by order and under circumstances of an exceptional nature, to be specified in such order, waive the whole or part of any interest payable under this section in respect of any warehoused goods:

Provided further that the Board may, if it is satisfied that it is necessary so to do in the public interest, by notification in the Official Gazette, specify the class of goods in respect of which no interest shall be charged under this section.

6. Relevant Points to be noted under Section 61

As per Budget 2002, 100% EOUs can deposit capital goods in the Bonded Warehouse for a period beyond 5 years with the permission from the department.

- Interest @ 15% is payable for the goods deposited beyond the permissible period. This is calculated on the amount of duty payable.
- No interest is payable when no duty is finally payable at the time of clearance from the warehouse [Pratibha Processors, 1996. S.C. and National Steel Industries Ltd. (H.C.) 2002].
- For perishable goods, the period of deposit may be 45 days or less.
- When the permission for extension was not granted, the importer has an option to prefer an appeal before CESTAT.

7. Warehousing—Grant of extension in the warehousing period under Section 61 of the Customs Act, 1962 after expiry of the warehousing period

1. Section 61 of the Customs Act, 1962 lays down the period for which the imported goods can be warehoused. The first proviso to this section provides that the period of warehousing prescribed, on sufficient cause being shown, can be extended for a period not exceeding 6 months by Commissioner of Customs. Further, extension in the period can be granted by the Chief Commissioner of Customs.

2. A doubt has arisen whether extension in the warehousing period can be granted when the application for extension is moved after the expiry of the initial or extended warehousing period. Section 61 of the Customs Act, 1962 is silent on this issue.

3. In order to arrive at a uniform practice in granting such extensions, the matter was examined in consultation with Ministry of Law. Consequently, it was been decided that the importers may be advised to file such applications for extensions in the warehousing period to the proper authority well before the expiry of initial/extended period of warehousing.

4. However, in cases of exceptional circumstances, the extensions in the warehousing period can be considered and granted even after the expiry of initial/extended warehousing period. In all such cases, the jurisdictional Chief Commissioner may himself decide the request for extension after taking into consideration the exceptional circumstances, the nature of the commodity, the rate of duties, particularly, whether the same results in loss of revenue to the government, the licensing aspects involved etc. [M.F. (D.R.) Circular No. 12/98-Cus., dated 6.3.1998].

8. Control over Warehoused Goods

Section 62 provides that all warehoused goods shall be subject to the control of the proper officer [Section 62(1)].

No person shall enter a warehouse or remove any goods therefrom without the permission of the proper officer [Section 62(2)].

The proper officer may cause any warehouse to be locked with the lock of the Customs Department and no person shall remove or break such lock [Section 62(3)].

The proper officer shall have access to every part of warehouse and power to examine the goods therein [Section 62(4)].

9. Payment of Rent and Warehouse Charges

Section 63 stipulates that the owner of any warehoused goods shall pay to the warehouse keeper rent and warehouse charges at the rates fixed under any law for the time being in force or where no rates are so fixed at such rates as may be fixed by the Commissioner of Customs [Section 63(1)].

If any rent or warehouse charges are not paid within ten days from the date when they become due, the warehousekeeper, may, after notice to the owner of the warehoused goods, and with the permission of the proper officer, cause to be sold (any transfer of the warehoused goods notwithstanding) such sufficient portion of the goods as the warehousekeeper may select. [Section 63(2)].

Failure to pay warehouse charges will attract interest @24%.

10. Owner's Right to Deal with Warehoused Goods

With the sanction of the proper officer, and on payment of the prescribed fees, the owner of any goods may either before or after warehousing the same:

- (a) inspect the goods,
- (b) separate damaged or deteriorated goods from the rest,
- (c) sort the goods or change their containers for the purpose of preservation, sale, export or disposal of the goods,
- (d) deal, with the goods and their containers in such manner as may be necessary to prevent loss or deterioration or damage to the goods,
- (e) show the goods for sale,
- (f) take samples of goods without entry for home consumption and if the proper officer permits, without payment of duty on such samples. (Section 64).

11. Manufacture and other operations in relation to Goods in a Warehouse

The owner of any warehoused goods may carry on any manufacturing process or other operations in the warehouse in relation to such goods, with the sanction of Assistant or Deputy Commissioner of Customs and subject to such conditions and on payment of such fees as may be prescribed [Section 65(1)].

Where in the course of any operations permissible in relation to any warehoused goods under Sub-section (1) there is any waste or refuse, the following provisions will apply:

- (a) if the whole or any part of the goods resulting from such operations are exported, import duty shall be remitted on the quantity of the goods contained in so much of the waste or refuse as has arisen from the operations carried on in relation to the goods exported, provided that such waste or refuse is either destroyed or duty is paid on such waste or refuse as if it had been imported into India in that form;
- (b) if the whole or any part of the goods resulting from such operation are cleared from the warehouse for home consumption, import duty shall be charged on the quantity of the warehoused goods contained in so much of waste or refuse as has arisen from the operations carried on in relation to the goods cleared for home consumption [Section 62(2)].

Example:

To illustrate, let us take the case of manufacture of stainless steel articles in a bonded warehouse out of imported stainless steel sheets.

1. Suppose 10 tonnes of stainless steel sheets of assessable value ₹ 4.000 per tonne attracting duty at 300% under heading 7219 or 7220 of Customs Tariff, plus Additional duty (Countervailing duty) under 7212 of Central Excise Tariff at ₹ 500/-per tonne + 5% of ₹ 500/- per tonne (A) have been imported.

The amount of duty leviable works out to ₹ 1,25,250, the importer pays 50% of the duty assessed and gives a bond for twice the balance amount before depositing the goods in the bonded warehouse.

Suppose 9 tonnes of stainless steel articles are manufactured in bond and one tonne of scrap has resulted as waste from the manufacture. (B)

Suppose 75% of the manufactured articles (6.75 tonnes) is exported to foreign countries. (C)

Suppose the remaining 25% of the articles manufactured (2.25 tonnes) is cleared for home consumption. (D)

The waste of one tonne (B) above is to be apportioned in the ratio (C): (D), i.e. 750 kg. of steel scrap is relatable to exports of finished articles and 250 kg. to the clearances of finished articles of home consumption.

Suppose 375 kg. out of the 750 kg. of scrap is destroyed under Customs supervision. Then no duty is leviable on the imported steels contained in this quantity.

Suppose the remaining 375 kg. of scrap relating to exports is cleared for home consumption. Then duty is leviable on this quantity of scrap on the value of such scrap (say ₹ 1,000 per tonne) at the rate of duty of 300% as applicable to steel-other (Scrap) under heading 7219.90 Customs Tariff [instead of at the rate indicated at (A) above on the imported stainless steel sheets].

On the 250 kg. of scrap relating to the finished products cleared for home consumption, the full duty applicable to the imported goods on value of the imported goods indicated at (A) above should be collected irrespective of whether the scrap is destroyed or cleared for home consumption.

As far as the imported material contained in the finished articles (D) cleared for home consumption is concerned, duty is leviable at the rate prevailing at the time of clearance for stainless steel sheets on the value indicated at (A) above (Section 68 of the Customs Act).

As far as the imported material contained in the exported finished articles (c) is concerned, no duty is leviable. (Section 69 of the Customs Act).

12. Power to Exempt Imported Materials used in the Manufacture of Goods in Warehouse

Under Section 66, if any imported materials are used in accordance with the provisions of Section 65 for the manufacture of any goods and the rate of duty leviable on the imported materials exceeds the rate of duty leviable on such goods, the Central Government, if satisfied that in the interest of the establishment or development of any domestic industry, it is necessary, so to do, may, by notification in the Official Gazette, exempt the imported materials from the whole or part of the excess rate of duty.

13. Removal of Goods from one Warehouse to another

The owner of any warehoused goods may with the permission of the proper officer, remove them from one warehouse to another subject to such conditions as may be prescribed for the due arrival of the warehoused goods at the warehouse to which removal is permitted. (Section 67).

14. The Central Board of Revenue has framed the Warehoused Goods (Removal) Regulations, 1963 for this purpose providing for the following:

(a) Conditions for transport of warehoused goods in the same town — Where the goods are to be removed from one warehouse to another in the same town, proper officer may require that the transport of the goods between the two warehouses be under the supervision of an officer of customs, the owner meeting the cost of such supervision.

(b) Conditions for transport of warehoused goods to another town — Where the goods are to be removed from one warehouse to another in a different town the proper officer may require the person requesting removal to execute a bond in a sum equal to the amount of import duty leviable on such goods and in such form and manner as the proper officer deems fit.

(c) Terms of the bond to be executed — The terms of the bond shall be that if the person executing the bond produces to the proper officer, within three months or within such extended period as such officer may allow, a certificate issued by the proper officer at the place of destination that the goods have arrived at that place the bond shall stand discharged but otherwise an amount equal to the import duty leviable on the goods in respect of which the said certificate is not produced shall stand forfeited.

(d) Surety or security to be furnished — The proper officer may require that the bond shall be with such surety or security or both as is acceptable to him.

15. Clearance of Warehoused goods for Home Consumption

Under Section 68, the importer of any warehoused goods may clear them for home consumption, if:

- (a) a bill of entry for home consumption in respect of such goods has been presented in the prescribed form;
- (b) the import duty leviable on such goods and all penalties, rent, interest and other charges payable in respect of such goods have been paid; and
- (c) an order for clearance of such goods for home consumption has been made by the proper officer.

Provided that the owner of any warehoused goods may, at any time before an order for clearance of goods for consumption has been made in respect of such goods, relinquish his title to the goods upon payment of rent, interest, other charges and penalties that may be payable in respect of the goods and upon such relinquishment, he shall not be liable to pay duty thereon.

Provided further that the owner of any such warehoused goods shall not be allowed to relinquish his title to such goods regarding which an offence appears to have been committed under this Act or any other law for the time being in force.

In the recent Supreme Court case, [BICCO Lawrie Ltd. 2008, (S.C.)] it was held that once assessment of warehoused goods is complete and duty liability is discharged, the goods are no longer warehoused goods even-though they are further retained in the warehouse.

In this case the goods (kerosene) were assessed and duty paid. But the goods were not removed from the warehouse. There was a change in the tariff rate at the time of actual removal and the department demanded the duty as per the increased rate. Held that once assessment was over and duty liability was discharged, no further assessment is necessary and no further liability arises.

16. Clearance of Warehoused Goods for Exportation

Any warehoused goods may be exported to a place outside India without payment of import duty, if:

- (a) a shipping bill or a bill of export has been presented in respect of such goods in the prescribed form;
- (b) the export duty, penalties, rent, interest and other charges payable in respect of such goods have been paid; and

- (c) an order for clearance of such goods, for exportation has been made by the proper officer [Section 69(1)].

Section 69(2) lays down that notwithstanding anything contained in Sub-section (1), if the Central Government is of the opinion that warehoused goods of any specified description are likely to be smuggled back into India, it may, by notification in the Official Gazette, direct that such goods shall not be exported to any place outside India without payment of duty or may be allowed to be so exported subject to such restrictions and conditions as may be specified in the notification.

Under Section 15(1)(b), the rate of duty applicable to warehoused goods (as and when cleared for home consumption) is the rate of duty prevailing on the date of actual removal of the goods from the warehouse. Hence, the warehouse keeper or Bond Officer endorses the date (or dates) on which the goods are physically removed from the warehouse. If any further duty has become due on account of a change in the rates of duty before such removal, the Bond Clerk who receives the duplicate bill of entry from the warehouse keeper initiates necessary action. More than one clearance of a single warehoused consignment can also be effected by filing different bills of entry (Green Bill of Entry) under Section 68. As far as the rate of exchange (applied for conversion of value declared in foreign currency to Indian currency for collection of duty, on the value) is concerned, the same exchange rate that prevailed and applied for conversion on the date of filing of the warehousing (info-bond) bill of entry by the importer is applicable to all clearances ex-bond.

17. Warehoused Goods Cleared after the Expiry of Warehousing Period — Relevant Date for Determining Customs Duty

Board's instructions as contained in F. No. 473/206/87-Cus.-VII, dated 12.7.1989 on the above mentioned subject clarified that on expiry of the permissible or extended warehousing period the goods kept in the warehouse cease to be warehoused goods and, therefore, their removal from the warehouse cannot be covered by the provisions of Section 15(1)(b) of the Customs Act. It was also noted that there was no specific legal provision to determine the rate of duty in such cases of warehoused goods where the bond period has expired. It was accordingly concluded that the residual clause of Section 15(1)(c) of the Customs Act could apply after expiry of the warehousing period and that the rate of duty in such cases shall be rate prevalent on the date of payment of duty.

The issue has been re-considered in the light of Hon'ble Supreme Court's judgment (in Civil Appeal No. 4459 of 1989) delivered on August 23rd, 1996 in the case of *Kesoram Rayon v. Commissioner of Calcutta*, 1996 (86) E.L.T. 464 (S.C.), 1996 (66) ECR 201 (SC) report. In the said judgement the Hon'ble Apex Court has held that goods which are not removed from a warehouse within the permissible or extended period are to be treated as goods. Importer is required to pay the full amount of duty chargeable at the rate applicable on the date of their deemed removal from the warehouse, that is, the date on which the permitted or extended period expired.

In other words, a clear interpretation of the Hon'ble Supreme's Court's judgement is that the date of payment of duty in the case of warehoused goods removed after the expiry of the permissible or extended period would henceforth be the date of

expiry of the warehousing period or such other extended period as the case may be and not the date of payment of duty. [C.B.E. & C. Circular No. 31/97-Cus., dated 14.8.1997].

18. Allowance in case of Volatile Goods

When any warehoused goods to which this section (Section 70) applies are at the time of delivery from a warehouse found to be deficient in quantity on account of natural loss, the Assistant / Deputy Commissioner of Customs may remit the duty on such deficiency [Section 70(1)].

Sub-section (2) of Section 70 lays down that this section applies to such warehoused goods as the Central Government, having regard to the volatility of the goods and the manner or their storage, may, by notification in the Official Gazette specify.

The Government has issued Notification No. 122/63 Cus. dt. 11.5.1963 (as amended), under Sub-section (2), which details such goods namely:

- (1) aviation fuel, motor spirit, mineral turpentine, acetone, menthol, raw naphtha, vaporising oil, kerosene, high speed diesel oil, batching oil, diesel oil, furnace oil and ethylene dichloride kept in tanks and liquid helium gas kept in containers;
- (2) wine, spirit and beer, kept in casks,

to which the provisions of this section shall apply when they are deposited in a warehouse.

The above provisions in the Customs Act however does not preclude the application of Sections 22 and 23 to warehoused goods (viz.) for remission of Customs duty on damaged and deteriorated goods and on lost, destroyed and abandoned goods. When any warehoused goods are damaged at any time before clearance for home consumption on account of an account not due to any wilful act, negligence or default of the owner, proportionate abatement of duty is available to the importer. Similarly when any warehoused goods have been lost or destroyed at any time before clearance for home consumption, remission of duty can be allowed by the Assistant Commissioner.

When all the imported goods warehoused have been cleared for home consumption on payment of duty or exported or otherwise duly accounted for, the bond furnished by the importer under Section 59 is cancelled and returned to the importer.

19. Procedure for taking out removal of goods from warehouse

Section 71 provides that no warehoused goods shall be taken out of a warehouse except on clearance for home consumption or re-exportation or for removal to another warehouse or as otherwise provided by this Act.

20. Goods improperly removed from warehouse etc.

Section 72 lays down provisions in respect of goods improperly removed from warehouse etc.

In any of the following cases, that is to say —

- (a) Where any warehoused goods are removed from a warehouse in contravention of Section 71;
- (b) Where any warehoused goods have not been removed from a warehouse at the expiration of the period during which such goods are permitted under Section 61 to remain in a warehouse;
- (c) Where any warehoused goods have been taken under Section 64 as samples without payment of duty;
- (d) Where any goods in respect of which a bond has been executed under Section 59 and which have not been cleared for home consumption or exportation are not duly accounted for to the satisfaction of the proper officer;

the proper officer may demand and the owner of such goods forthwith pay the full amount of duty chargeable on account of such goods, together with all penalties, rent, interest, and other charges payable in respect of such goods [Section 72(1)];

If any owner fails to pay amount demanded under Sub-section (1), the proper officer may, without prejudice to any other remedy, cause to be detained and sold, after notice to the owner (any transfer of the goods notwithstanding) such sufficient portion of his goods, if any, in the warehouse, as the said officer may select.

21. Cancellation and Return of Warehousing Bond

Section 73 lays down that when the whole of goods covered by any bond executed under Section 59 have been cleared for home consumption or exported or are otherwise duly accounted for and when all amounts due on account of such goods have been paid, the proper officer shall cancel the bond as discharged in full and shall on demand deliver it, so cancelled, to the person who had executed or is entitled to receive it.

7.32 Adjudication and Appellate Provisions

Orders passed by adjudicating authorities give rise to disputes between the assessee and Customs Department. These generally arise in connection with the classification and valuation of goods or in regard to infraction of legal provisions and/or procedures. In any tax system, disputes are bound to arise howsoever simple a tariff is made to appear. *Burkets famous diction that it is difficult to tax and please, is known to all.*

An incorrect assessment to a duty might take place on account of various factors. It may arise due to inadvertence, error, collusion, or misconstruction on the part of an officer of revenue, or through mis-statement as to the quantity, description or value in respect of dutiable goods on the part of an assessee. *An incorrect assessment is as detrimental to the exchequer as it is to the assessee.* There are various factors leading to a mistake which result in an incorrect assessment. The Public Accounts Committee [(5th Lok Sabha) (1972-73) 89th Report at P. 14] identified them as mainly resulting from.

7.32.1 Appellate Procedures

The procedure prescribed for filing appeals and revision applications against orders passed by Customs officers are described in Sections 128, 130 and 131 of the Customs Act.

The relevant provisions regarding Appeal and Revision are discussed below, Section-wise.

(A) Appeals to Commissioner (Appeals)(Section 128)

- (1) Any person aggrieved by any decision or order passed under this Act by an officer of customs lower in rank than a Commissioner of Customs may appeal to the Commissioner (Appeals) within 60 days from the date of communication to him of such decision or order:

Provided that the Commissioner (Appeals) may, if he is satisfied that the appellant was prevented by sufficient cause from presenting the appeal within the aforesaid period of 60 days, allow it to be presented within a further period of thirty days.

- (2) Every appeal under this section, shall be in such form and shall be verified in such manner as may be specified by rules made in this behalf.

Procedure in Appeal (Section 128A)

- (1) The Commissioner (Appeals) shall give an opportunity to the appellant to be heard if he so desires.
- (2) The Commissioner (Appeals) may, at the hearing of an appeal, allow the appellant to go into any ground of appeal not specified in the grounds of appeal, if the Commissioner (Appeal), is satisfied that the omission of that ground from the grounds of appeal was not willful or unreasonable.
- (3) The Commissioner (Appeals) shall, after making such further inquiry as may be necessary, pass such order as he thinks just and proper, confirming, modifying or annulling the decision or order appealed against.

Provided that an order enhancing any penalty or fine in lieu of confiscation or confiscating goods of greater value or reducing the amount of refund shall not be passed unless the appellant has been given a reasonable opportunity of showing cause against the proposed order;

Provided further that where the Commissioner (Appeals) is of opinion that any duty has not been levied or has been short-levied or erroneously refunded, no order requiring the appellant to pay any duty not levied, short-levied and erroneously refunded shall be passed unless the appellant is given notice within the time-limit specified in Section 28 to show cause against the proposed order.

- (4) The order of the Commissioner (Appeals) disposing of the appeal shall be in writing and shall state the points for determination, the decision thereon and the reasons for the decision.

- (4A) The Commissioner (Appeals) shall, where it is possible to do so, hear and decide every appeal within a period of six months from the date on which it is filed.
- (5) On the disposal of the appeal, the Commissioner (Appeals) shall communicate the order passed by him to the appellant, the adjudicating authority and the Commissioner of Customs.

(B) Appellate Tribunal (Section 129)

- (1) The Central Government shall constitute an Appellate Tribunal to be called the Customs, Excise and Service Tax Appellate Tribunal consisting of as many judicial and technical members as it thinks fit to exercise the powers and discharge the functions conferred on the Appellate Tribunal by this Act.
- (2) A judicial member shall be a person who has for at least ten years held a judicial office in the territory of India or who has been a member of the Indian Legal Service and has held a post in Grade I of that service or any equivalent or higher post for at least three years, or who has been an advocate for at least ten years.

Explanation: For the purposes of this sub-section—

- (i) in computing the period during which a person has held judicial office in the territory of India, there shall be included any period, after he has held any judicial office, during which the person has been an advocate or has held the office of a member of a Tribunal or any post, under the Union or a State, requiring special knowledge of law;
 - (ii) in computing the period during which a person has been an advocate, there shall be included any period during which the person has held a judicial office or the office of a member of a Tribunal or any post, under the Union or a State, requiring special knowledge of law after he became an advocate.
- (2A) A technical member shall be a person who has been a member of the Indian Customs and Central Excise Service, Group A, and has held the post of Commissioner of Customs or Central Excise or any equivalent or higher post for at least three years.
 - (3) The Central Government shall appoint—
 - (a) a person who is or has been a Judge of a High Court; or
 - (b) one of the members of the Appellate Tribunal, to be the President thereof.
 - (4) The Central Government may appoint one or more members of the Appellate Tribunal to be the Vice-President, or, as the case may be, Vice-Presidents, thereof.
 - (4A) Omitted by Finance Act, 2003.
 - (5) Vice-President shall exercise such of the powers and perform such of the functions of the President as may be delegated to him by the President by a general or special order in writing.

Appeals to the Appellate Tribunal (Section 129A)

- (1) Any person aggrieved by any of the following orders may appeal to the Appellate Tribunal against such order:
- (a) a decision or order passed by the Commissioner of Customs as an adjudicating authority;
 - (b) an order passed by the Commissioner (Appeals) under Section 128A;
 - (c) an order passed by the Board or the Appellate Commissioner of Customs under Section 128, as it stood immediately before the appointed day;
 - (d) an order passed by the Board or the Commissioner of Customs, either before or after the appointed day, under Section 130, as it stood immediately before that day:

Provided that no appeal shall lie to the Appellate Tribunal and the Appellate Tribunal shall not have jurisdiction to decide any appeal in respect of any order referred to in clause (b), if such order relates to:

- (a) any goods imported or exported as baggage;
- (b) any goods loaded in a conveyance for importation into India, but which are not unloaded at their place of destination in India, or so much of the quantity of such goods as has not been unloaded at any such destination if goods unloaded at such destination are short of the quantity required to be unloaded at that destination;
- (c) payment of drawback as provided in Chapter X, and the rules made thereunder;

Provided further that the Appellate Tribunal may, in its discretion, refuse to admit an appeal in respect of an order referred to in clause (b) or clause (c) or (d) where:

- (i) the value of the goods confiscated without option having been given to the owner of the goods to pay a fine in lieu of confiscation under Section 125; or
 - (ii) in any disputed case other than a case where the determination of any question having a relation to the rate of duty of customs or to the value of goods for purposes of assessment is in issue or is one of the points in issue, the difference in duty involved or the duty involved; or
 - (iii) the amount of fine or penalty determined by such order, does not exceed Fifty thousand rupees.
- (1A) Every appeal against any order of the nature referred to in the first proviso to Sub-section (1), which is pending immediately before the commencement of Section 40 of the Finance Act, 1984, before the Appellate Tribunal and any matter arising out of or connected with such appeal and which is so pending shall stand transferred on such commencement to the Central Government under Section 129DD as if such appeal or matter were an application or a matter arising out of an application made to it under that section.
- (1B) The Board may, by notification in the Official Gazette constitute such

committees as may be necessary for the purpose of this Act, consisting of two Chief Commissioners or Commissioners of Customs.

- (2) The Committee of Commissioners of Customs may, if it is of opinion that an order passed by the Appellate Commissioner of Customs under Section 128 as it stood immediately before the appointed day, or by the Commissioner (Appeals) under Section 128A, is not legal or proper, direct the proper officer to appeal on its behalf to the Appellate Tribunal against such order.

Provided that where the Committee of Commissioners of Customs differs in its opinion regarding the appeal against the order of the Commissioner (Appeals), it shall state the point or points on which it differs and make a reference to the jurisdictional Chief Commissioner of Customs who shall, after considering the facts of the order, if it is of the opinion that the order passed by the Commissioner (Appeals) is not legal or proper, direct the proper officer to appeal to the Appellate Tribunal against such order.

Explanation: For the purposes of this sub-section, "jurisdictional Chief Commissioner" means the Chief Commissioner of Customs having jurisdiction over the adjudicating authority in the matter.

- (3) Every appeal under this section shall be filed within three months from the date on which the order sought to be appealed against is communicated to the Commissioner of Customs, or as the case may be, the other party preferring the appeal.
- (4) On receipt of notice that an appeal has been preferred under the section, the party against whom the appeal has been preferred may, notwithstanding that he may not have appealed against such order or any part thereof, file, within forty-five days of the receipt of the notice, a memorandum of cross-objections verified in such manner as may be specified by rules made in this behalf against any part of the order appealed against and such memorandum shall be disposed of by the Appellate Tribunal as if it were an appeal presented within the time specified in Sub-section (3).
- (5) The Appellate Tribunal may admit an appeal or permit the filing of a memorandum of cross-objections after the expiry of the relevant period referred to in Sub-section (3) or Sub-section (4), if it is satisfied that there was sufficient cause for not presenting it within that period.
- (6) An appeal to the Appellate Tribunal shall be in such form and shall be verified in such manner as may be specified by rules made in this behalf and shall, irrespective of the date of demand of duty and interest or of levy of penalty in relation to which the appeal is made, be accompanied by a fee of:
 - (a) where the amount of duty and interest demanded and penalty levied by any officer of customs in the case to which the appeal relates is five lakh rupees or less, one thousand rupees;
 - (b) where the amount of duty and interest demanded and penalty levied by any officer of customs in the case to which the appeal relates is more

than five lakh rupees, but not exceeding fifty lakh rupees, five thousand rupees;

- (c) where the amount of duty and interest demanded and penalty levied by any officer of customs in the case to which the appeal relates is more than fifty lakh rupees, ten thousand rupees:

Provided that no such fee shall be payable in the case of an appeal referred to in Sub-section (2) or a memorandum of cross-objections referred to in Sub-section (4).

- (7) Every application made before that Appellate Tribunal,-
- (a) in an appeal for grant of stay or for rectification of mistake or for any other purpose; or
- (b) for restoration of an appeal or an application,
- shall be accompanied by a fee of five hundred rupees.

Orders of Appellate Tribunal (Section 129B)

- (1) The Appellate Tribunal may, after giving the parties to the appeal an opportunity of being heard, pass such orders thereon as it thinks fit, confirming, modifying or annulling the decision or order appealed against or may refer the case back to the authority which passed such decision or order with such directions as the Appellate Tribunal may think fit, for a fresh adjudication or decision, as the case may be, after taking additional evidence, if necessary.
- (2) The Appellate Tribunal may, at any time within six months from the date of the order, with a view to rectifying any mistake apparent from the record, amend any order passed by it under Sub-section (1) shall make such amendments if the mistake is brought to its notice by the Commissioner of Customs or the other party to the appeal:

Provided that an amendment which has the effect of enhancing the assessment or reducing a refund or otherwise increasing the liability of the other party shall not be made under this sub-section, unless the Appellate Tribunal has given notice to him of its intention to do so and has allowed him a reasonable opportunity of being heard.

- (2A) The Appellate Tribunal shall, where it is possible to do so, hear and decide every appeal within a period of three years from the date on which such appeal is filed:

Provided that where an order of stay is made in any proceeding relating to an appeal filed under Sub-section (1) of Section 129A, the Appellate Tribunal shall dispose of the appeal within a period of one hundred and eighty days from the date of such order:

Provided further that if such appeal is not disposed of within the period specified in the first proviso, the stay order shall, on the expiry of that period, stand vacated.

- (3) The Appellate Tribunal shall send a copy of every order passed under this section to the Commissioner of Customs and the other party to the appeal.
- (4) Save as otherwise provided in Section 130 or Section 130E, order passed by the Appellate Tribunal on appeal shall be final.

Procedure of Appellate Tribunal (Section 129C)

- (1) The powers and functions of the Appellate Tribunal may be exercised and discharged by Benches constituted by the President from amongst the members thereof.
- (2) Subject to the provisions contained in Sub-section (4), a Bench shall consist of one judicial member and one technical member.
- (3) Omitted by Finance Act, 1995.
- (4) The President or any other member of the Appellate Tribunal authorised in this behalf by the President may, sitting singly, dispose of any case which has been allotted to the Bench of which he is a member where —
 - (a) the value of the goods confiscated without option having been given to the owner of the goods to pay a fine in lieu of confiscation under Section 125; or
 - (b) in any disputed case other than a case where the determination of any question having a relation to the rate of duty of customs or to the value of goods for purposes of assessment is in issue or is one of the points in issue, the difference in duty involved or the duty involved; or
 - (c) the amount of fine or penalty involved;
does not exceed Ten Lakh rupees.
- (5) If the members of a Bench differ in opinion on any point, the point shall be decided according to the opinion of the majority, if there is a majority; but if the members are equally divided, they shall state the point or points on which they differ and make a reference to the President who shall either hear the point or points himself or refer the case for hearing on such point or point by one or more of the other members of the Appellate Tribunal and such point or points shall be decided according to the opinion of the majority of these members of the Appellate Tribunal who have heard the case, including those who first heard it.
- (6) Subject to the provisions of this Act, the Appellate Tribunal shall have power to regulate its own procedure and the procedure of the Benches thereof in all matters arising out of the exercise of its powers or of the discharge of its functions, including the places at which the Benches shall hold their sittings.
- (7) The Appellate Tribunal shall, for the purposes of discharging its functions, have the same powers as are vested in a court under the Code of Civil Procedure, 1908 (5 of 1908) when trying a suit in respect of the following matters, namely:
 - (a) discovery and inspection;

- (b) enforcing the attendance of any person and examining him on oath;
 - (c) compelling the production of books of account and other documents; and
 - (d) issuing commissions.
- (8) Any proceedings before the Appellate Tribunal shall be deemed to be a judicial proceeding within the meaning of Sections 193 and 228 and for the purpose of Section 196 of the Indian Penal Code (45 of 1860), and the Appellate Tribunal shall be deemed to be a Civil Court for all the purpose of Section 195 and Chapter XXVII of the Code of Criminal Procedure, 1973 (2 of 1974).

7.33 Powers of Committee of Chief Commissioners of Customs or Commissioners of Customs to pass certain orders (Section 129D)

- (1) The Committee of Chief Commissioners may, of its own motion, call for and examine the record of any proceeding in which a Commissioner of Customs as an adjudicating authority has passed any decision or order under this Act for the purpose of satisfying itself as to the legality or propriety of any such decision or order and may, by order, direct such Commissioner or any other Commissioner to apply to the Appellate Tribunal for the determination of such points arising out of the decision or order as may be specified by the Committee of Chief Commissioners in its order.

Provided that where the Committee of Chief Commissioners of Customs differs in its opinion as to the legality or propriety of the decision or order of the Commissioner of Customs, it shall state the point or points on which it differs and make a reference to the Board. After considering the facts of the decision or order passed by the Commissioner of Customs, if the board is of the opinion that the decision or order passed by the Commissioner of Customs is not legal or proper, it may direct such Commissioner or any other Commissioner to make an appeal to the Appellate Tribunal for the determination of such points arising out of the decision or order.

- (2) The Commissioner of Customs may, of his own motion, call for and examine the record of any proceedings in which an adjudicating authority subordinate to him has passed any decision or order under this Act for the purpose of satisfying himself as to the legality or propriety of any such decision or order and may, by order, direct such authority to apply to the Commissioner (Appeals) for the determination of such points arising out of the decision or order as may be specified by the Commissioner of Customs in his order.
- (3) Every order under Sub-section (1) or Sub-section (2), shall be made within a period of three months from the date of communication of the decision or order of the adjudicating authority.
- (4) Where in pursuance of an order under Sub-section (1) or Sub-section (2), the adjudicating authority or any officer of customs authorised in this behalf by the Commissioner of Customs, makes an application to the Appellate Tribunal or the Commissioner (Appeals) within a period of three months from the date of communication of the order under Sub-section (1) or Sub-

section (2) to the adjudicating authority, such application shall be heard by the Appellate Tribunal or the Commissioner (Appeals), as the case may be, as if such application were an appeal made against the decision or order of the adjudicating authority and the provisions of this Act regarding appeals, including the provisions of Sub-section (4) of Section 129A shall, so far as may be, apply to such application.

7.34 Section 129DD. Revision by Central Government

- (1) The Central Government may, on the application of any person aggrieved by any order passed under Section 128A, where the order is of the nature referred to in the first proviso to Sub-section (1) of Section 129A, annul or modify such order.

Provided that the Central Government may in its discretion refuse to admit an application in respect of an order where the amount of duty or fine or penalty, determined by such order does not exceed five thousand rupees.

Explanation: For the purposes of this sub-section. "Order passed under Section 128A" includes an order passed under that section before the commencement of Section 40 of the Finance Act, 1984, against which an appeal has not been preferred before such commencement and could have been, if the said section had not come into force, preferred after such commencement, to the Appellate Tribunal.

- (1A) The Commissioner of Customs may, if he is of the opinion that an order passed by the Commissioner (Appeals) under Section 128A is not legal or proper direct the proper officer to make an application on his behalf to the Central Government for revision of such order.
- (2) An application under Sub-section (1) shall be made within three months from the date of the communication to the applicant of the order against which the application is being made:

Provided that the Central Government may, if it is satisfied that the applicant was prevented by sufficient cause from presenting the application within the aforesaid period of three months, allow it to be presented within a further period of three months.

- (3) An application under Sub-section (1) shall be in such form and shall be verified in such manner as may be specified by rules made in this behalf and shall be accompanied by a fee of:
- (a) two hundred rupees, where the amount of duty and interest demanded, fine or penalty levied by an officer of customs in the case to which the application relates is one lakh rupees or less;
- (b) one thousand rupees, where the amount of duty and interest demanded, fine or penalty levied by an officer of customs in the case to which the application relates is more than one lakh rupees:

Provided that no such fee shall be payable in the case of an application referred to in Sub-section (1A).

- (4) The Central Government may, of its own motion, annul or modify any order referred to in Sub-section (1).
- (5) No order enhancing any penalty or fine in lieu of confiscation or confiscating goods of greater value shall be passed under this section—
 - (a) in any case in which an order passed under Section 128A has enhanced any penalty or fine in lieu of confiscation or has confiscated goods of greater value, and
 - (b) in any other case, unless the person affected by the proposed order has been given notice to show cause against it within one year from the date of the order sought to be annulled or modified.
- (6) Where the Central Government is of opinion that any duty of customs has not been levied or has been short-levied, no order levying or enhancing the duty shall be made under this section unless the person affected by the proposed order is given notice to show cause against it within the time limit specified in Section 28.

7.35 Section 130E. Appeal to Supreme Court

An appeal shall lie to the Supreme Court from—

- (a) any judgment of the High Court delivered in any case which, on its own motion or on an oral application made by or on behalf of the party aggrieved, immediately after the passing of the judgment, the High Court certifies to be a fit one for appeal to the Supreme Court; or
- (b) any order passed before the establishment of the National Tax Tribunal by the Appellate Tribunal relating, among other things, to the determination of any question having a relation to the rate of duty of customs or to the value of goods for purposes of assessment.

Section 130F. Hearing before Supreme Court

- (1) The provisions of the Code of Civil Procedure, 1908 (5 of 1908), relating to appeals to the Supreme Court shall, so far as may be, apply in the case of appeals under Section 130E as they apply in the case of appeals from decrees of a High Court:

Provided that nothing in this Sub-section shall be deemed to affect the provisions of Section 131.

- (2) The costs of the appeal shall be in discretion of the Supreme Court.
- (3) Where the judgment of the High Court is varied or reversed in the appeal effect shall be given to the order of the Supreme Court in the case of a judgment of the High Court.

7.36 Section 129E. Deposit, pending appeal, of duty and Interest demanded or penalty levied

Where in any appeal under this Chapter, the decision or order appealed against

relates to any duty and interest demanded in respect of goods which are not under the control of the customs authorities or any penalty levied under this Act, the person desirous of appealing against such decision or order shall, pending the appeal, deposit with the proper officer, the duty and interest demanded or the penalty levied:

Provided that where in any particular case, the Commissioner (Appeals) or the Appellate Tribunal is of opinion that the deposit of duty and interest demanded or penalty levied would cause undue hardship to such person, the Commissioner (Appeals) or, as the case may be, the Appellate Tribunal, may dispense with such deposit subject to such conditions as he or it may deem fit to impose so as to safeguard the interests of revenue.

Provided further that where an application is filed before the Commissioner (Appeals) for dispensing with the deposit of duty and interest demanded or penalty levied under the first proviso, the Commissioner (Appeals) shall, where it is possible to do so, decide such application within thirty days from the date of its filing.

7.37 Section 129EE: Interest on delay payment of Refund

Where an amount deposited by the appellant in pursuance of an order passed by the Commissioner (Appeals) or the appellate authority, under the first proviso to section 129E, is required to be refunded consequent upon the order of the appellate authority and such amount is not refunded *within three months* from the date of communication of such order to the adjudicating authority, unless the operation of the order of the appellate authority is stayed by a superior court or tribunal, there shall be paid to the appellant interest at the rate specified in section 27A after the expiry of three months from the date of communication of the order of the appellate authority, till the date of refund of such amount.

[Section 130, 130A, 130B, 130C and 130D are omitted by National Tax Tribunal Act, 2005 with effect from a date yet to be notified].

7.38 Section 131. Sums due to be paid notwithstanding reference, etc.

Notwithstanding that a reference has been made to the High Court or the Supreme Court or an appeal has been preferred to the Supreme Court, under this Act before the commencement of the National Tax Tribunal Act, 2005, sums due to the Government as a result of an order passed under Sub-section (1) of Section 129B shall be payable in accordance with the order so passed.

7.39 Section 131A. Exclusion of time taken for copy

In computing the period of limitation, specified for an appeal or application under this Chapter, the day on which the order complained of was served, and if the party preferring the appeal or making the application was not furnished with a copy of the order when the notice of the order was served upon him, the time requisite for obtaining a copy of such order shall be excluded.

7.40 Section 131B. Transfer of certain pending proceedings and transitional provisions

- (1) Every appeal which is pending immediately before the appointed day before

the Board under Section 128, as it stood immediately before that day, and any matter arising out of or connected with such appeal and which is so pending shall stand transferred on that day to the Appellate Tribunal and the Appellate Tribunal may proceed with such appeal or matter from the stage at which it was on that day:

Provided that the appellant may demand that before proceeding further with that appeal or matter, he may be re-heard.

- (2) Every proceeding which is pending immediately before the appointed day before the Central Government under Section 131, as it stood immediately before that day, and any matter arising out of or connected with such proceeding and which is so pending shall stand transferred on that day to the Appellate Tribunal and the Appellate Tribunal may proceed with such proceeding or matter from the stage at which it was on that day as if such proceeding or matter were an appeal filed before it:

Provided that, if any such proceeding or matter relates to an order where—

- (a) the value of the goods confiscated without option having been given to the owner of the goods to pay a fine in lieu of confiscation under Section 125; or
- (b) in any disputed case, other than a case where the determination of any question having a relation to the rate of duty of customs or to the value of goods for purposes of assessment is in issue or is one of the points in issue, the difference in duty involved or the duty involved; or
- (c) the amount of fine or penalty determined by such order, does not exceed ten thousand rupees, such proceeding or matter shall continue to be dealt with by the Central Government as if the said Section 131 had not been substituted:

Provided, further that the applicant or the other party may make a demand to the Appellate Tribunal that before proceeding further with that proceeding or matter, he may be re-heard.

- (3) Every proceeding which is pending immediately before the appointed day before the Board or the Commissioner of Customs under Section 130, as it stood immediately before that day, and any matter arising out of or connected with such proceeding and which is so pending shall continue to be dealt with by the Board or the Commissioner of Customs, as the case may be, as if the said section had not been substituted.
- (4) Any person who immediately before the appointed day was authorised to appear in any appeal or proceeding transferred under Sub-section (1) or Sub-section (2) shall, notwithstanding anything contained in Section 146A, have the right to appear before the Appellate Tribunal in relation to such appeal or proceeding.

7.41 Appeal not to be filed in certain cases (Section 131BA)

Section 131BA provides that notwithstanding the fact that no appeal, application, revision or reference has been filed by the Commissioner of customs against any

decision or order passed under the provisions of the act pursuant to the order or instruction or direction issued by the board. Then—

- (a) no person, being a party in appeal, application, revision or reference shall contend that the commissioner of customs has acquiesced in the decision on the disputed issue by not filing appeal, application, revision or reference; and
- (b) the appellate tribunal or court hearing an appeal, application, revision or reference shall have regard to the circumstances under which the appeal, application, revision or reference was not filed by the commissioner of customs in pursuance of order or instruction or direction by the board.

Section 131C. Definitions

In this Chapter—

- (a) “Appointed day” means the date of coming into force of the amendment to this Act specified in Part I of the Fifth Schedule to the Finance (No. 2) Act, 1980;
- (b) [Omitted by Section 30 read with Schedule to the National Tax Tribunal Act, 2005.]
- (c) “President” means the President of the Appellate Tribunal.

7.42 Customs (Appeals) Rules, 1982

In exercise of the powers conferred by Sub-section (1) of Section 156 of the Customs Act, 1962 (52 of 1962) the Central Government hereby makes the following rules (effective from 11.10.1982) namely:-

CHAPTER II

Appeals to Commissioner (Appeals)

Rule 3. Form of Appeal to Commissioner (Appeals):

- (1) An appeal under Sub-section (1) of Section 128 to the Commissioner (Appeals) shall be made in Form No. C.A.-1.
- (2) The grounds of appeal and the form of verification as contained in Form No. C.A.-1 shall be signed:
 - (a) in the case of an individual, by the individual himself or where the individual is absent from India, by the individual concerned or by some person duly authorised by him in this behalf and where the individual is a minor or is mentally incapacitated from attending to his affairs, by his guardian or by any other person competent to act on his behalf;
 - (b) in the case of a Hindu undivided family, by the Karta, and, where the Karta is absent from India or is mentally incapacitated from attending to his affairs, by any other adult member of such family;
 - (c) in any case of a company or local authority, by the principal officer thereof;
 - (d) in the case of a firm, by any partner thereof, not being a minor;

- (e) in the case of any other person, by that person or some person competent to act on his behalf,
- (3) The form of appeal in Form No. C.A.-1 shall be filed in duplicate and shall be accompanied by a copy of the decision or order appealed against.

Rule 4. Form of application to the Commissioner (Appeals):

- (1) An application under Sub-section (4) of Section 129D to the Commissioner (Appeals) shall be made in Form No. C.A.-2.
- (2) The form of application in Form No. C.A.-2 shall be filed in duplicate and shall be accompanied by two copies of the decision or order passed by adjudicating authority (one of which at least shall be a certified copy) and a copy of the order passed by the Commissioner of Customs directing such authority to apply to the Commissioner (Appeals).

Rule 5. Production of additional evidence before the Commissioner (Appeals):

- (1) The appellant shall not be entitled to produce before the Commissioner (Appeals) any evidence, whether oral or documentary, other than the evidence produced by him during the course of proceedings before the adjudicating authority, except in the following circumstances, namely:
 - (a) where the adjudicating authority has refused to admit evidence which ought to have been admitted; or
 - (b) where the appellant was prevented by sufficient cause from producing the evidence which he was called upon to produce by that authority; or
 - (c) where the appellant was prevented by sufficient cause from producing before the authority any evidence which is relevant to any ground of appeal; or
 - (d) where the adjudicating authority has made the order appealed against without giving sufficient opportunity to the appellant to adduce evidence relevant to any ground of appeal.
- (2) No evidence shall be admitted under Sub-rule (1) unless the Commissioner (Appeals) records in writing the reasons for its admission.
- (3) The Commissioner (Appeals) shall not take any evidence produced under sub-rule (1) unless the adjudicating authority or an officer authorised in this behalf by the said authority has been allowed a reasonable opportunity:
 - (a) to examine the evidence or documents or to cross-examine any witness produced by the appellant; or
 - (b) to produce any evidence or any witness in rebuttal of the evidence produced by the appellant under Sub-rule (1).
- (4) Nothing contained in this rule shall affect the powers of the Commissioner (Appeals) to direct the production of any document, or the examination of any witness, to enable him to dispose of the appeal.

CHAPTER III**Appeals to Appellate Tribunal****Rule 6. Form of appeals, etc. to the Appellate Tribunal**

- (1) An appeal under Sub-section (1) of Section 129A to the Appellate Tribunal shall be made in Form No. C.A.-3.
- (2) A memorandum of cross-objections to the Appellate Tribunal under Sub-section (4) of Section 129A shall be made in Form No. C.A.- 4.
- (3) Where an appeal under Sub-section (1) of Section 129A or a memorandum of cross-objections under Sub-section (4) of that section is made by any person other than the Commissioner of Customs, the grounds of appeal, the grounds of cross-objections and the forms of verification as contained in Form Nos. C.A.-3 and C.A.-4 as the case may be, respectively shall be signed by the person specified in Sub-rule (2) of Rule 3.
- (4) The form of appeal in Form No. C.A.-3 and the form of memorandum of cross-objections in Form No. C.A.-4 shall be filed in quadruplicate and shall be accompanied by an equal number of copies of the order appealed against (one of which at least shall be a certified copy).

Rule 7. Form of application to the Appellate Tribunal:

- (1) An application under Sub-section (4) of Section 129D to the Appellate Tribunal shall be made in Form No.C.A.-5.
- (2) The form of application in Form No. C.A.-5 shall be filed in quadruplicate and shall be accompanied by an equal number of copies of the decision or order passed by the Commissioner of Customs (one of which at least shall be a certified copy) and a copy of the order passed by the Board directing such Commissioner to apply to the Appellate Tribunal.

Rule 8. Form of application to the High Court:

- (1) An application under Sub-section (1) of Section 130A requiring the High Court to direct the Appellate Tribunal to refer to the High Court any question of law shall be made in Form No. CA-6 and such application shall be filed in quadruplicate.
- (2) A memorandum of cross-objections under Sub-section (3) of Section 130A to the High Court shall be made in Form No. CA-7 and such memorandum shall be filed in quadruplicate.
- (3) Where an application under Sub-section (1) of Section 130A or a memorandum of cross-objections under Sub-section (3) of that section is made by any person other than the Commissioner of Customs, the application, the memorandum or form of verification, as the case may be, contained in Form No. CA-6 or Form No. CA-7 shall be signed by the person specified in sub-rule (2) of Rule 3.

CHAPTER IIIA
Revision by Central Government

Rule 8A. Form of revision application to the Central Government:

- (1) A revision application under Sub-section (1) of Section 129DD to the Central Government shall be in Form No. C.A.-8.
- (2) The grounds of revision application and the form of verification as contained in Form C.A.-8 shall be signed by the person specified in Sub-rule (2) of Rule 3.
- (3) Where the revision application is signed by the authorised representative of the applicant, the document authorising such representative to sign and appear on behalf of the applicant shall be appended to such revision application.
- (4) The revision application in Form No. C.A.-8 shall be filed in duplicate and shall be accompanied by an equal number of copies of the following documents, namely:
 - (i) order passed by the Commissioner of Customs (Appeals) under Section 128A; and
 - (ii) decision or order passed by the Customs Officer which was the subject matter of the order referred to in clause (i).

Rule 8B. Procedure for filing revision application:

- (1) The revision application in Form C.A.-8 shall be presented in person to the Under Secretary, Revision Applications, Ministry of Finance, Department of Revenue, Central Secretariat, New Delhi - 1, or sent by registered post addressed to said Under Secretary.
- (2) The revision application send by registered under Sub-rule (1), shall be deemed to have been submitted on the date on which it is received in the office of the said Under Secretary.

In *Collector of Customs, Bombay v. Bharat Vijay Mills* [1986 (7) AIR 186] the CEGAT has held that if an assessment is not appealed against, it becomes final and cannot be modified. This is a very important decision and has to be kept in mind for ensuring that the doors to re-assessment by revision are not closed for all time by inaction to lodge appropriate proceedings in time.

CHAPTER IV
Authorised Representative

Rule 9. Qualifications for authorised representatives:

For the purposes of Section 146A, an authorised representative shall include a person who has acquired any of the following qualifications, being the qualifications specified under Clause (d) of Sub-section (2) of the said Section 146A, namely:

- (a) a Chartered Accountant within the meaning of the Chartered Accountants Act, 1949 (38 of 1949); or

- (b) a Cost Accountant within the meaning of the Cost and Works Accountants Act, 1959 (23 of 1959); or
- (c) a Company Secretary within the meaning of the Company Secretaries Act, 1980 (56 of 1980), who has obtained a certificate of practice under Section 6 of that Act; or
- (d) a post-graduate or an Honours degree holder in Commerce or a post-graduate degree or diploma holder in Business Administration from any recognised University; or
- (e) a person formerly employed in the Department of Customs or Central Excise or Narcotics and has retired or resigned from such employment after having rendered service in any capacity in one or more of the said Departments for not less than ten years in the aggregate.

Explanation: In this rule, "Recognised University" means any of the Universities specified below, namely:

- I. *Indian Universities:* Any Indian University incorporated under any law for the time being in force in India;
- II. *Rangoon University*
- III. *English and Walsh Universities:* The Universities of Birmingham, Bristol, Cambridge, Durham, Leeds, Liverpool, London, Manchester, Oxford, Reading, Sheffield and Wales;
- IV. *Scottish Universities:* The Universities of Aberdeen, Edinburgh, Glasgow and St. Andrews;
- V. *Irish Universities:* The Universities of Dublin (Trinity College), the Queen's University, Belfast and the National University of Dublin;
- VI. *Pakistan Universities:* Any Pakistan University incorporated under any law for the time being in force;
- VII. *Bangladesh Universities:* Any Bangladesh University incorporated under any law for the time being in force.

Rule 10. Authority under Section 146A(5)(b):

The Commissioner of Customs having jurisdiction in the proceedings in which a person who is not a legal practitioner is found guilty of misconduct in connection with that proceeding under the Act shall be the authority for the purpose of clause (b) of Sub-section (5) of Section 146A.

7.43 Settlement Commission

Rules for Settlement of Cases

Consequent upon the constitution of the Settlement Commission as stated above, the rules pertaining to the matters relating to Settlement of cases both under Central Excise (Rules 220, 220A to 220C) and Customs (Customs Settlement of

Cases) Rules, 1999 have been notified separately vide Notification Nos. 55/99-CE(N.T.) and 59/99-CUS(N.T.) both dated 22.10.1999, respectively. These rules inter alia provides for the procedure of making an application before the Settlement Commission and the Forms to be used for the same including various disclosures of information required to be made and fee etc. to be paid. The two sets of rules relevant to Central Excise and Customs are on the same lines and for that reason only the Rules framed under the Customs Act, i.e., Customs (Settlement of Cases) Rules, 1999 are reproduced hereunder in full whereas text of Rules 220, 220A to 220C and its annexures may be referred from the latest Central Excise Manual or any standard text book.

7.43.1 Customs and Central Excise Settlement Commission Procedure, 2007

[Ministry of Finance (Department of Revenue), Notification No. 1/2007/S.C.(PB), dated May 31, 2007.]

G.S.R. 406(E).—In exercise of the powers conferred by sub-section (4) of section 32(1) of the Central Excise Act, 1944 and sub-section (4) of section 127F of the Customs Act, 1962, in supersession of the Customs and Central Excise Settlement Commission Procedure, 1999 notified vide Notification dated the 26th October, 1999, except as respects things done or omitted to be done before such supersession, the Customs and Central Excise Settlement Commission hereby makes the following procedure, namely:-

1. Short title and commencement

(1) This procedure may be called the Customs and Central Excise Settlement Commission Procedure, 2007.

(2) It shall come into force on the 1st day of June, 2007.

2. Definitions

Unless the context otherwise requires:

- (a) "applicant" means a person who makes an application to the Commission under sub-section (1) of section 32E of the Central Excise Act or under sub-section (1) of section 127B of the Customs Act;
- (b) "authorised representative" means:
 - (a) in relation to an applicant, except where such applicant is required by the Commission to attend in person, a person who would be entitled to represent himself before any Central Excise and Customs Authority of under Section 35Q of the Central Excise Act or section 146A of the Customs Act.
 - (b) in relation to a Commissioner, a person—
 - (i) authorized in writing by the Commissioner or the Chief Commissioner, or
 - (ii) appointed by the Central Government authorized representative or authorized by the Central Board of Excise and Customs to appear,

plead and act for the Commissioner in any proceeding before the Commission;

- (c) "Central Excise Act" means the Central Excise Act, 1944 (1 of 1944);
- (d) "Commission" means the Customs and Central Excise Settlement Commission instituted under section 32 of Central Excise Act, and includes any Bench exercising or discharging the powers or functions of the Commission;
- (e) "Customs Act" means the Customs Act, 1962 (52 of 1962);
- (f) "Secretary" means the Secretary of the Commission and includes an Administrative Officer;
- (g) "settlement application" means an application made by a person to the Commission under sub-section (1) of section 32E of Central Excise or under sub-section (1) of section 127B of the Customs Act, as the case may be, to have a case relating to him settled;
- (h) all other words and expressions used herein and not defined but defined in the Central Excise Act and the Customs Act, shall have the same meaning respectively assigned to them in the said Acts.

3. Language of the Commission

- (i) all the pleadings before the Commission may, at the option of the applicant, be in Hindi or in English;
- (ii) all orders and other proceedings of the Commission may, at the opinion of the Commission, be in Hindi or in English.

4. Signing of notices, etc.

- (i) any requisition, direction, letter, authorization, order or written notice to be issued by the Commission shall be signed by the Chairman or a Vice-Chairman or any other Member of the Commission or by the Secretary;
- (ii) nothing in sub-rule (1) shall apply to any requisition or direction which the Commission may, in the course of the hearing, issue to an applicant or a Commissioner or an authorized representative personally.

5. Procedure for filing settlement application

(1) A settlement application shall be presented by the applicant in person to the Secretary at the headquarters of the Commission at New Delhi or of the Bench within whose jurisdiction his case falls or to any officer authorized in this behalf by the Secretary, or shall be sent by registered post addressed to the Secretary.

(2) A settlement application sent by post under sub-rule (1) shall be deemed to have been presented to the Secretary on the day on which it is received in the office of the Commission.

6. Preparation of paper books etc.

- (1) If the applicant or the Commissioner, as the case may be, proposes to refer

or rely upon any documents or statements or other papers, he may submit six copies of a paperbook containing such papers duly indexed and paged within seven days from the date of issuance of notice under sub-section (1) of section 32F of the Central Excise Act or sub-section (1) of section 127C of the Customs Act, as the case may be:

Provided that if the Commission is satisfied that there is sufficient reason for delay, it may condone the delay and admit the paperbook.

(2) If the applicant proposes to refer to or rely upon any documents or statements or other papers during the course of hearing under sub-section (5) of section 32F of Central Excise Act or sub-section (5) of section 127C of the Customs Act, as the case may be the applicant may submit six copies of a paperbook containing such papers duly indexed and paged, within thirty days or within such extended period as may be allowed by the Commission, of the receipt of an order passed or date of deemed admission under sub-section (1) of section 32F of the Central Excise Act or sub-section (1) of section 127C of the Customs Act, as the case may be.

(3) If the Commissioner proposes to refer to or rely upon any documents or statements or other papers during the course of hearing under sub-section (5) of section 32F of the Central Excise Act or sub-section (5) of section 127C of Customs Act, as the case may be the Commissioner may submit six copies of a paperbook containing such papers duly indexed and paged, within thirty days or within such extended period as may be allowed by the Commission, of the receipt of an order passed or date of deemed admission under sub-section (1) of section 32F of the Central Excise Act or sub-section (1) of section 127C of the Customs Act, as the case may be.

(4) The Commission may, suo motu, direct the preparation of six copies of a paperbook by and at the cost of the applicant or the Commissioner, containing copies of such statements, documents and papers, as it may consider necessary for the proper disposal of the settlement application on or matters arising therefrom.

(5) The papers referred to in sub-rules (1), (2), (3) and (4) must be legibly written or type-written in double space or printed. If Xerox copy of the document is filed, then the same should be legible. Each paper should be certified as a true copy by the party filing the same and indexed in such a manner as to give a brief description of the documents, with page numbers and the authority before whom it was filed.

7. Filing of Affidavit

Where a fact which is not borne out by or is contrary to the record relating to the case, is alleged in the settlement application, it shall be stated clearly and concisely and supported by a duly sworn affidavit.

8. Date and place of hearing of application to be notified

The Commission shall notify to the applicant and the Commissioner the date and place of hearing of the application.

9. Sitting of Bench

A Bench shall hold its sittings at its headquarters. The Bench may, however, at

the discretion of the Presiding Officer, hold its sittings at any place in its jurisdiction notified by the Commission.

10. Power of a Bench

A Bench shall dispose of such, settlement applications or matters arising therefrom as the Chairman may by general or special order direct.

11. Constitution of Special Bench

(1) The Chairman may, for the disposal of a particular case, constitute a Special Bench consisting of at least five Members taken from all the Benches of the Commission.

(2) The Special Bench shall be presided over by the Chairman or a Vice-Chairman.

(3) If the Members of the Special Bench are equally divided, they shall state the point or points or which they differ and make a reference to the Chairman who shall refer the case for hearing on such point or points by one or more of other members of the Settlement Commission and such point or points shall be decided according to the opinion of the majority of the Members of the Settlement Commission who have heard the case.

(4) Notwithstanding anything contained in the foregoing provisions of this rule, if one or more persons constituting the Special Bench (whether such person is the Presiding Officer or another Member of the Special Bench) are unable to function in the Special Bench owing to illness or any other cause or in the event of occurrence of a vacancy either in the office of the Presiding Officer or in the office of one or other Members of the Special Bench, the remaining Members, if more than three may function as the Special Bench, and the senior most of the remaining Members shall act as the Presiding Officer of the Special Bench.

12. Filing of authorization

An authorised representative appearing for the applicant at the hearing of an application shall file before the commencement of the hearing a document authorising him to appear for the applicant and if he or she is a relative of the applicant, the document shall state the nature of his or her relationship with the applicant, or if he or she is a person regularly employed by the applicant, the capacity in which he or she is at the time employed.

13. Verification of additional facts

Where in the course of any proceedings before the Commission any facts not contained in the settlement application (including the annexure and the statements and other documents accompanying such annexure) are sought to be relied upon, they shall be submitted to the Commission in writing and shall be verified in the manner as provided for in the settlement application.

14. Proceedings not open to the public

The proceedings before the Commission shall not be open to the public and no person (other than the applicant, his employee, the concerned officers of the Commission or the Customs and Central Excise Department or the authorized

representatives) shall, without the permission of the Commission remain present during such proceedings.

15. Publication of orders of the Special Bench

The Chairman may, at his discretion, direct the publication of orders or portions containing the rulings of the Special Bench with such modifications as to names and other particulars therein, as he or she may deem fit.

16. Adjournment of hearing

The Commission may, on such terms as it thinks fit and at any stage of the proceedings, adjourn the hearing of the application or any matters arising therefrom.

F.No. 16/Tech/2007-SC(PB)

A.K. Gupta
Secy., Settlement Commission, Customs and
Central Excise, Principal Bench

7.44 Search, Seizure, Arrest, Confiscation etc.

Introduction

The Customs Law seeks to regulate imports and exports. It is, therefore, necessary for the customs Department to be fully equipped to meet situations where there is any illegal export or import of goods. In any fiscal enactment, it is common to find provisions relating to searches, seizure and arrest. These provisions only advance the primary objective of the law namely "Prevention of illegal imports and exports. At the same time, it should be remembered that the Customs Act does not aim at detection of a crime. The Customs Officers are also not primarily concerned with the detection and punishment of a crime but they are entrusted in ensuring that there is no smuggling of contraband articles. They are to safeguard recovery of customs duty properly applicable to the goods. Chapter XIII of the Act consisting of Sections 100 to 110 contain detailed provisions in regard to searches, seizure and arrest. These are discussed below:

(A) Power to search suspected persons entering or leaving India

Under Section 100 of the Act where the proper officer of the Customs has reason to believe that the following categories of persons have secreted any goods, liable to confiscation or any documents thereto, he may search such persons.

The categories of persons referred to in the above paragraph are: -

- (a) any person who has landed from or is about to board, or is on board any vessel within the Indian Customs waters;
- (b) any person who has landed from or is about to board, or is on board a foreign-going aircraft;
- (c) any person who has got out of, or is about to get into, or is in vehicle, which has arrived from, or is to proceed to any place outside India;
- (d) any person not included in clauses (a), (b) or (c) who has entered or is about to leave India;
- (e) any person in a customs area.

(B) Power to search suspected persons in certain other cases

Under Section 101 of the Act, an officer of the Customs empowered generally or specially by an order of Commissioner of Customs can search any person if he has reason to believe that any person has secreted about his person, the following goods which are liable to confiscation, or documents relating thereto:

- (a) gold;
- (b) diamonds;
- (c) manufactures of gold or diamond;
- (d) watches;
- (e) any other class of goods which the Central Government may, by notification in the Official Gazette, specify.

The power under Section 101 is without prejudice to the power conferred under Section 100 of the Act. Again under Section 101 any person can be searched.

(C) Persons to be searched may require to be taken before Gazetted Officer of Customs or Magistrate

Section 102 of the Act provides that when any officer of Customs is about to search any person in terms of Sections 100 and 101, he shall, if such person so requires, take him without unnecessary delay to the nearest Gazetted Officer of customs or magistrate. If such requisition is made, the officer of customs may detain the person making it until, he can bring him before the gazetted officer of customs or the magistrate. The Gazetted Officer of customs or the magistrate before whom any "such person is brought shall, if he sees no reasonable ground for search, forthwith discharge the person. In other cases, he shall direct that a search be made. Before making a search, the officer of Customs shall call upon two or more persons to attend and witness the search and may issue an order in writing to them or any of them so to do. The search would be made in the presence of such persons and a list of all things seized in the course of such search shall be prepared by such officer or other person and signed by such witnesses. Where the person to be searched is a female, the search shall be done only by a female.

(D) Power to screen or X-Ray bodies of suspected persons for detecting secreted goods

Section 103 of the Act contains powers, to screen or X-Ray bodies of persons suspected of secreting certain goods liable to confiscation. Under this section, detention of a person and production without unnecessary delay before the nearest Magistrate by the proper officer is envisaged. The Magistrate before whom any person is brought shall, if he sees how reasonable ground for believing that such person has any such goods secreted inside his body, forthwith discharge such person. On the other hand, where the Magistrate has reasonable ground for believing that any such person has any such goods liable for confiscation secreted in his body and the Magistrate is satisfied that an X-Ray is necessary for this purpose, he may make an order to a radiologist possessing qualifications recognised by the

Central Government for the purpose of screening or X-raying the body of any person, such person would be taken to a radiologist for the purpose of screening or X-raying the body. The radiologist shall, after the screening or X-Ray, forward his report together with the X-Ray picture taken by him to the Magistrate without unnecessary delay. On receipt of the report of radiologist, if the Magistrate is satisfied that any person has any goods liable to confiscation secreted inside his body, he may direct; that suitable action for bringing out such goods be taken on the advice and under the supervision of a registered medical practitioner and such person shall be bound to comply with such direction. In the case of a female, the advice and supervision of a female registered medical practitioner is required. For the purposes of complying with the provisions of this section any person brought before the Magistrate may be detained by him for such period as the Magistrate may direct.

The above provisions will not apply to any such person who admits that goods liable to confiscation are secreted in his body and who voluntarily submits himself for suitable action being taken for bringing out such goods.

(E) Power to arrest

Section 104 of the Act empowers the Commissioner to authorise any officer of Customs by general or special order to arrest any person if such officer has reason to believe that any person in India or within the Indian Customs waters has committed an offence punishable under Section 132 or Section 133 or Section 135 or Section 135A or Section 136. As soon as arrest is made the grounds of his arrest must be indicated to him and the person arrested shall be taken without unnecessary delay to a Magistrate. For the purposes of releasing such person on bail or otherwise, the officer of (customs who has arrested any person shall have the same powers and be subject to the same provisions as the officer-in-charge of a police station under the Code of Criminal Procedure, 1898. In regard to the statements made by a person arrested before the Customs Officer, it was held in *State of Punjab v. Burkat Ram*, "AIR 1962 SC 276, that the Customs Officer under the Sea Customs Act was not a police officer within the meaning of Section 25 of the Evidence Act. Therefore, the statements made by the person arrested have been held not covered by Section 25 of the Indian Evidence Act - *Illias v. Collector of Customs, Madras*, AIR 1970 SC 1065. The Bombay High Court in *Pukhraj Panna Lal Shah v. K. K. Gangauli* held that confessional statement made before the Customs Officer are not to be hit by Section 25 of the Evidence Act.

Section 132 deals with false declaration false documents etc. Section 133 deals with obstruction of officers of customs. Section 135 deals with evasion of duty or prohibitions. Section 135A provides for punishment for preparation to export goods in contravention of the provisions of the Act.

(F) Bail not to be granted in certain cases without hearing public prosecutor Section 104A:

(1) Notwithstanding anything contained in the Code of Criminal Procedure, 1973, no person accused of an offence punishable for a term of imprisonment of three years or more under section 135 shall be released on bail or on his own bond unless—

- (i) The public prosecutor has been given an opportunity to oppose the application for such release; and

- (ii) where the public prosecutor opposes the application, the Magistrate is satisfied that there are reasonable grounds for believing that he is not guilty of such offence and that he is not likely to commit any offence while on bail:

Provided that a person who is under the age of eighteen years or is a woman or is sick or infirm, may be released on bail if the Magistrate so directs.

(2) Notwithstanding anything contained in the Code of Criminal Procedure, 1973, no police officer shall, save as otherwise provided under this Act, investigate into an offence under this Act unless specifically authorized by the Central Government by a general or special order, and subject to such conditions as **may be specified in the order.**

(G) Power to search premises

Section 105 of the Act deals with it. The Assistant/Deputy Commissioner of Customs or any other officer of customs in case of any area adjoining the land frontier or the coast of India specially empowered by name in this behalf by the Board, if he has reason to believe that any goods liable to confiscation or any documents or things which in his opinion will be useful to any proceedings under the Act, are secreted in any place, he may authorise any officer of customs to search or may himself search for such goods, documents, or things. For the purposes of conducting such a search, the provisions of the Code of Criminal Procedure, 1973 relating to searches would apply.

(H) Power to stop and search conveyances

Section 106 of the Act deals with it. Accordingly, where the proper officer has reason to believe that any aircraft, vehicle or animal in India or any vessel in India or within the Indian customs waters has been, is being, or is about to be, used in the smuggling of any goods or in the carriage of any goods which have been smuggled, he may at any time stop any such vehicle, animal or vessel or, in the case of an aircraft, compel it to land, and

- (a) rummage and search any part of the aircraft, vehicle or vessel;
- (b) examine and search any goods in the aircraft, vehicle or vessel or on the animal;
- (c) break open the lock of any door or package for exercising the powers conferred by clauses (a) and (b), if the keys are withheld.

(2) Where for the above purpose—

- (a) it becomes necessary to stop any vessel or compel any aircraft to land, it shall be lawful for any vessel or aircraft in the service of the Government while flying her proper flag and any authority authorised in this behalf by the Central Government to summon such vessel to stop or the aircraft to land, by means of an international signal, code or other recognised means, and thereupon such vessel shall forthwith stop or such aircraft shall forthwith land; and if it fails to do so, chase may be given thereto by any vessel or aircraft as aforesaid and if after a gun is fired as a signal the vessel fails to stop or the aircraft fails to land, it may be fired upon;
- (b) it becomes necessary to stop any vehicle or animal, the proper officer may use all lawful means for stopping it, and where such means fail, the vehicle or animal may be fired upon.

(I) Power to inspect

Section 106A of the Act empowers an Officer of Customs to enter any place intimated under Chapter IVA or IVB of the Act and inspect the goods kept or stored therein and require any person found therein, who is for the time being in charge thereof, to produce to him for this inspection the accounts maintained under the said Chapter IVA or Chapter IVB and to furnish to him such other information as he may reasonably require for the purpose of ascertaining whether or not such goods have been illegally imported, exported or likely to be illegally exported.

(J) Power to examine persons

Under Section 107 of the Act, any Officer of Customs empowered specially or generally by an order of the Commissioner of Customs may, during the course of any enquiry in connection with the smuggling of any goods —

- (a) require any person to produce or deliver any document or thing relevant to the enquiry;
- (b) examine any person acquainted with the facts and circumstances of the case.

(K) Power to summon persons to give evidence and produce documents

Section 108 of the Act deals with it. Accordingly, any Gazetted Officer of customs duty (the words “empowered by the Central Government”, has been omitted by Finance Act, 2008 w.e.f. 13th July 2006) shall have power to summon any person whose attendance he considers necessary either to give evidence or to produce a document or any other thing in any inquiry which such officer is making in connection with the smuggling of any goods.

A summons to produce documents or other things may be for the production of certain specified documents or things or for the production of all documents or things of a certain description in the possession or under the control of the person summoned.

All persons so summoned shall be bound to attend either in person or by an authorised agent, as such officer may direct; and all persons so summoned shall be bound to state the truth upon any subject respecting which they are examined or make statements and produce such documents and other things as may be required.

Provided that the exemption under Section 132 of the Code of Civil Procedure, 1908 (5 of 1908), shall be applicable to any requisition for attendance under this section.

Every such inquiry as aforesaid shall be deemed to be a judicial proceeding within the meaning of Section 193 and Section 228 of the Indian Penal Code, 1860 (45 of 1860).

(L) Power to require production of order permitting clearance of goods imported by land

Under Section 109 of the Act, any Officer of Customs appointed for any area adjoining the land frontier of India and “empowered generally or specially by an order

by the Board, may require any person in possession of any goods which such officer has reason to believe to have been imported into India by land, to produce the order made under Section 47 permitting clearance of the goods. The provisions of this section shall not apply to any imported goods passing from a land frontier to a land customs station by a route appointed under clause (c) of Section 7.

(M) Seizure of goods, documents and things

Under Section 110 of the Act, if the proper officer of Customs has reason to believe that any goods are liable to confiscation under the Act, he may seize such goods. Where it is not practicable to seize such goods, the proper officer may serve on the owner of the goods an order that he shall not remove, part with, or otherwise deal with the goods except with the previous permission of such officer.

The Central Government may, having regard to the perishable or hazardous nature of any goods, depreciation in the value of the goods with the passage of time, constraints of storage space for the goods or any other relevant considerations, by notification in the Official Gazette, specify the goods or class of goods which shall, as soon as may be, after its seizure under Sub-section (1), be disposed of by the proper officer in such manner as the Central Government may, from time to time, determine after following the procedure hereinafter specified.

In exercise of the powers conferred by Sub-section (1A) of Section 110 of the Customs Act, 1962 (52 of 1962), the Central Government, having regard to the perishable nature, depreciation in the value with the passage of time, constraints of storage space and valuable nature of the goods, has specified the following goods, namely:

1. Liquors;
2. Primary cells and primary batteries including re-chargeable batteries;
3. Wrist watches including electronic wrist watches; watch movements or components thereof;
4. All electronic goods including television sets, video cassette recorders, tape recorders, calculators, computers; components and spares thereof including diodes, transistors, integrated circuits etc; and
5. Dangerous drugs and psychotropic substances.”

Where any goods, being goods specified above have been seized by a proper officer under Sub-section (1), he shall prepare an inventory of such goods containing such details relating to their description, quality, quantity, mark, numbers, country of origin and other particulars as the proper officer may consider relevant to the identity of the goods in any proceedings under this Act and shall make an application to a Magistrate for the purpose of —

- (a) certifying the correctness of the inventory so prepared; or
- (b) taking, in the presence of the Magistrate, photographs of such goods and certifying such photographs as true; or
- (c) allowing to draw representative samples of such goods, in the presence of the Magistrate, and certifying the correctness of any list of samples so drawn.

Where any application is made as above, the Magistrate, shall allow the application.

Where any goods are seized and no notice in respect thereof is given under clause (a) of Section 124 within 6 months of seizure of the goods, the goods shall be returned to the person from whose possession they were seized. This period of 6 months however, can be extended by the Commissioner of Customs for a period not exceeding six months.

The proper officer may seize any documents or things which in his opinion, will be useful for, or relevant to, any proceeding under this Act. The person from whose custody any documents are seized is entitled to make copies thereof or take extracts therefrom in the presence of an officer of customs.

Section 110A: Any goods, documents or things seized under Section 110 may, pending the order of the adjudicating authority, be released to the owner on taking a bond from him in the proper form with such security and conditions as the adjudicating authority may require.

7.45 Confiscation of Goods

Goods become liable to confiscation if the Importer or Exporter contravenes any of the provisions of the Customs Act, 1962 or any other Act for the time being in force in relation to the importation and exportation of goods. Some of the more important allied statutes that get attracted in this manner are, to mention just a few, the Arms Act, the Copyright Act, the Dangerous Drugs Act, the Foreign Exchange Management Act, the Imports and Exports (Control) Act, the Trade Marks Act and the Ancient Monuments Preservation Act. The responsibility of the Officers of Customs to ensure that none of the provisions of these and such enactments is contravened, is thus onerous. It is also to meet that there are several instances of contraventions of these provisions and this has paved the way to procedures being laid down for, not only bringing the contraventions to the notice of those concerned, but also to take those responsible to task for non-compliance with statutory obligations. Of course, there are contraventions of the Customs Act, 1962 also and all these are taken care of by the set procedures for adjudication.

We have already seen that Section 28 of the Customs Act provides for a notice to be issued to the Importer or Exporter of any goods if duties of Customs have not been levied or have been short levied or erroneously refunded. Similarly, if any contravention of any provision of any Act for the time being in force is noticed, it is a statutory obligation placed on the Department that a notice of show cause be issued to the person concerned, so that he is given an opportunity to explain his side of the matter. Section 124 of the Customs Act lays down as follows:

(a) Confiscation of improperly imported goods etc.

Under Section 111, the following goods brought from a place outside India shall be liable to confiscation: -

- (a) any goods imported by sea or air which are unloaded or attempted to be unloaded at any place other than a customs port or customs airport appointed under clause (a) of Section 7 for the unloading of such goods;

- (b) any goods imported by land or inland water through any route other than a route specified in a notification issued under clause (c) of Section 7 for the import of such goods;
- (c) any dutiable or prohibited goods brought into any bay, gulf, creek or tidal river for the purpose of being landed at a place other than a customs port;
- (d) any goods which are imported or attempted to be imported or are brought within the Indian customs waters for the purpose of being imported, contrary to any prohibition imposed by or under this Act or any other law for the time being in force;
- (e) any dutiable or prohibited goods found concealed in any manner in any conveyance;
- (f) any dutiable or prohibited goods required to be mentioned under the regulations in an import manifest or import report which are not so mentioned;
- (g) any dutiable or prohibited goods which are unloaded from a conveyance in contravention of the provisions of Section 32, other than goods inadvertently unloaded but included in the record kept under Sub-section (2) of Section 45;
- (h) any dutiable or prohibited goods unloaded or attempted to be unloaded in contravention of the provisions of Section 33 or Section 34;
- (i) any dutiable or prohibited goods found concealed in any manner in any package either before or after the unloading thereof;
- (j) any dutiable or prohibited goods removed or attempted to be removed from a customs area or a warehouse without the permission of the proper officer or contrary to the terms of such permission;
- (k) any dutiable or prohibited goods imported by land in respect of which the order permitting clearance of the goods required to be produced under Section 109 is not produced or which do not correspond in any material particular with the specification contained therein;
- (l) any dutiable or prohibited goods which are not included or are in excess of those included in the entry made under this Act, or in the case of baggage in the declaration made under Section 77;
- (m) any goods which do not correspond in respect of value or in any other particular with the entry made under this Act or in the case of baggage with the declaration made under Section 77 in respect thereof, or in the case of goods under transshipment, with the declaration for transshipment referred to in the proviso to Sub-section (1) of Section 54.
- (n) any dutiable or prohibited goods transited with or without transshipment or attempted to be so transited in contravention of the provisions of Chapter VIII;
- (o) any goods exempted, subject to any condition, from duty or any prohibition in respect of the import thereof under this Act or any other law for the time being in force, in respect of which the condition is not observed, unless the non-observance of the condition was sanctioned by the proper officer;

- (p) any notified goods in relation to which any provisions of Chapter IVA or of any rule made under this Act for carrying out the purposes of that Chapter have been contravened.

(b) Penalty for improper importation of goods, etc.

Under Section 112, any person:

- (a) who, in relation to any goods, does or omits to do any act which act or omission would render such goods liable to confiscation under Section 111, or abets the doing or omission of such an act, or
- (b) who acquires possession of or is in any way concerned in carrying, removing, depositing, harbouring, keeping, concealing, selling or purchasing, or in any other manner dealing with any goods which he knows or has reason to believe are liable to confiscation under Section 111;

shall be liable:

- (i) in the case of goods in respect of which any prohibition is in force under this Act or any other law for the time being in force, to a penalty not exceeding the value of the goods or five thousand rupees, whichever is the greater;
- (ii) in the case of dutiable goods, other than prohibited goods, to a penalty not exceeding the duty sought to be evaded on such goods or five thousand rupees, whichever is the greater;
- (iii) in the case of goods in respect of which the value stated in the entry made under this Act or in the case of baggage, in the declaration made under Section 77 (in either case hereafter in this section referred to as the declared value) is higher than the value thereof, to a penalty not exceeding the difference between the declared value and the value thereof or five thousand rupees, whichever is the greater;
- (iv) in the case of goods falling both under clauses (i) and (ii), to a penalty not exceeding the value of the goods or the difference between the declared value and the value thereof or five thousand rupees, whichever is the highest;
- (v) in the case of goods falling both under clauses (ii) and (iii), to a penalty not exceeding the duty sought to be evaded on such goods or five times the difference between the declared value and the value thereof or five thousand rupees, whichever is the highest.

(c) Confiscation of goods attempted to be improperly exported, etc.

The following export goods shall be liable to confiscation, under Section 113 of the Act:

- (a) any goods attempted to be exported by sea or air from any place other than a customs port or a customs airport appointed for the loading of such goods;
- (b) any goods attempted to be exported by land or inland water through any route other than a route specified in a notification issued under clause (c) of Section 7 for the export of such goods;

- (c) any goods brought near the land frontier or the coast of India or near any bay, gulf, creek or tidal river for the purpose of being exported from a place other than a land customs station or a customs port appointed for the loading of such goods;
- (d) any goods attempted to be exported or brought within the limits of any customs area for the purpose of being exported, contrary to any prohibition imposed by or under this Act or any other law for the time being in force;
- (e) any goods found concealed in a package which is brought within the limits of a customs area for the purpose of exportation;
- (f) any goods which are loaded or attempted to be loaded in contravention of the provisions of Section 33 or Section 34;
- (g) any goods loaded or attempted to be loaded on any conveyance, or water-borne, or attempted to be water-borne for being loaded on any vessel, the eventual destination of which is a place outside India, without the permission of the proper officer;
- (h) any goods which are not included or are in excess of those included in the entry made under this Act, or in the case of baggage in the declaration made under Section 77;
- (i) any goods entered for exportation which do not correspond in respect of value or in any material particular with the entry made under this Act or in the case of baggage with the declaration made under Section 77;
- (j) any goods entered for exportation under claim for drawback which do not correspond in any material particular with any information furnished by the exporter or manufacturer under this Act in relation to the fixation of rate of drawback under Section 75.
- (k) any goods on which import duty has not been paid and which are entered for exportation under Section 74;
- (l) any goods cleared for exportation under a claim for drawback which are not loaded for exportation on account of any wilful act, negligence or default of the exporter, his agent or employee, or which after having been loaded for exportation are unloaded without the permission of the proper officer;
- (m) any specified goods in relation to which any provisions of Chapter IVB or of any rule made under this Act for carrying out the purposes of that Chapter have been contravened.

(d) Penalty for attempt to export goods improperly etc.

According to Section 114 any person who, in relation to any goods, does or omits to do, any act, which act or omission would render such goods liable to confiscation under Section 113, or abet the doing or omission of such an act, shall be liable:

- (i) in the case of goods in respect of which any prohibition is in force under this Act or any other law for the time being in force, to a penalty not exceeding three times the value of the goods as declared by the exporter or the value as determined under this Act, whichever is the greater;

- (ii) in the case of dutiable goods, other than prohibited goods, to a penalty not exceeding the duty sought to be evaded or five thousand rupees, whichever is the greater;
- (iii) in the case of any other goods, to a penalty not exceeding the value of the goods, as declared by the exporter or the value as determined under this Act, whichever is greater.

(e) Penalty for short-levy or non-levy of duty in certain cases

Section 114A inserted by the Finance (No. 2) Act, 1996 w.e.f. 28.9.96, prescribes a mandatory penalty equal to the duty or interest not levied, short levied, not paid or part paid or erroneously refunded by reason of collusion or wilful mis-statement or suppression of facts by the person liable to pay the duty. The section reads as under—

Where the duty has not been levied or has been short-levied or the interest has not been charged or paid or has not been part paid or the duty or interest has been erroneously refunded by reason of collusion or any wilful mis-statement or suppression of facts, the person who is liable to pay the duty or interest, as the case may be, as determined under Sub-section (2) of Section 28 shall also be liable to pay a penalty equal to the duty or interest so determined:

Provided that where such duty or interest, as the case may be, as determined under Sub-section (2) of Section 28, and the interest payable thereon under Section 28AB, is paid within thirty days from the date of the communication of the order of the proper officer determining such duty, the amount of penalty liable to be paid by such person under this section shall be twenty-five per cent of the duty or interest, as the case may be, so determined:

Provided further that the benefit of reduced penalty under the first proviso shall be available subject to the condition that the amount of penalty so determined has also been paid within the period of thirty days referred to in that proviso:

Provided also that where the duty or interest determined to be payable is reduced or increased by the Commissioner (Appeals), the Appellate Tribunal or, as the case may be, the court, then, for the purposes of this section, the duty or interest as reduced or increased, as the case may be, shall be taken into account.

Provided also that in case where the duty or interest determined to be payable is increased by the Commissioner (Appeal), the Appellate Tribunal or, as the case may be, the court, then, the benefit of reduced penalty under the first proviso shall be available if the amount of the duty or the interest so increased, along with the interest payable thereon under Section 28AB, and twenty-five per cent of the consequential increase in penalty have also been paid within thirty days of the communication of the order by which such increase in the duty or interest takes effect:

Provided also that where any penalty has been levied under this section, no penalty shall be levied under Section 112 or Section 114.

Explanation — For the removal of doubts, it is hereby declared that:

- (i) the provisions of this section shall also apply to cases in which the order determining the duty or interest under Sub-section (2) of Section 28 relates

to notices issued prior to the date on which the Finance Act, 2000 receives the assent of the President;

- (ii) any amount paid to the credit of the Central Government prior to the date of communication of the order referred to in the first proviso or the fourth proviso shall be adjusted against the total amount due from such person.

(f) Penalty for use of false and incorrect material

Section 114AA provides that if a person knowingly or intentionally makes, signs or uses, or causes to be made, signed or used, any declaration, statement or document which is false or incorrect in any material particular, in the transaction of any business for the purposes of this Act, shall be liable to a penalty not exceeding five times the value of goods.

(g) Confiscation of conveyances

(1) The following conveyances shall be liable to confiscation, under Section 115:

- (a) any vessel which is or has been within the Indian customs waters, any aircraft which is or has been in India, or any vehicle which is or has been in a customs area, while constructed, adapted, altered or fitted in any manner for the purpose of concealing goods;
- (b) any conveyance from which the whole or any part of the goods is thrown overboard, staved or destroyed so as to prevent seizure by an officer of customs;
- (c) any conveyance which having been required to stop or land under Section 106 fails to do so, except for good and sufficient cause;
- (d) any conveyance from which any warehoused goods cleared for exportation, or any other goods cleared for exportation under a claim for drawback, are unloaded, without the permission of the proper officer;
- (e) any conveyance carrying imported goods which has entered India and is afterwards found with the whole or substantial portion of such goods missing, unless the master of the vessel or aircraft is able to account for the loss of, or deficiency in, the goods.

(2) Any conveyance or animal used as a means of transport in the smuggling of any goods or in the carriage of any smuggled goods shall be liable to confiscation, unless the owner of the conveyance or animal proves that it was so used without the knowledge or connivance of the owner himself, his agent, if any, and the person in charge of the conveyance or animal.

Provided that where any such conveyance is used for the carriage of goods or passengers for hire, the owner of any conveyance shall be given an option to pay in lieu of the confiscation of the conveyance a fine not exceeding the market price of the goods which are sought to be smuggled or the smuggled goods, as the case may be.

“Market price” in this section, means market price at the date when the goods are seized. (Explanation added to the section).

(h) Penalty for not accounting for goods

Under Section 116, if any goods loaded in a conveyance for importation into India, or any goods transhipped under the provisions of this Act or coastal goods carried in a conveyance, are not unloaded at their place of destination in India, or if the quantity unloaded is short of the quantity to be unloaded at that destination, and if the failure to unload or the deficiency is not accounted for to the satisfaction of the Assistant or Deputy Commissioner of Customs, the person-in-charge of the conveyance shall be liable:

- (a) in the case of goods loaded in a conveyance for importation into India or goods transhipped under the provisions of this Act, to a penalty not exceeding twice the amount of duty that would have been chargeable on the goods not unloaded or the deficient goods, as the case may be, had such goods been imported;
- (b) in the case of coastal goods, to a penalty not exceeding twice the amount of export duty that would have been chargeable on the goods not unloaded or the deficient goods, as the case may be, had such goods been exported.

(i) Penalties for contravention, etc., not expressly mentioned

Any person who contravenes any provision of this Act or abets any such contravention or who fails to comply with any provisions of this Act, with which it was his duty to comply, where no express penalty is elsewhere provided for such contravention or failure, shall be liable to a penalty not exceeding one lakh rupees (Section 117).

(j) Confiscation of packages and their contents

- (a) Where any goods imported in a package are liable to confiscation, the package and any other goods imported in that package shall also be liable to confiscation.
- (b) Where any goods are brought in a package within the limits of a customs area for the purpose of exportation and are liable to confiscation, the package and any other goods contained therein shall also be liable to confiscation (Section 118).

(k) Confiscation of goods used for concealing smuggled goods

Any goods used for concealing smuggled goods shall also be liable to confiscation, in terms of Section 119.

“Goods” does not include a conveyance used as a means of transport.

(l) Confiscation of smuggled goods notwithstanding any change in form, etc.

- (1) Smuggled goods may be confiscated notwithstanding any change in their form.
- (2) Where smuggled goods are mixed with other goods in such manner that the smuggled goods cannot be separated from such other goods, the whole of the goods shall be liable to confiscation.

Provided that where the owner of such goods proves that he had no knowledge or reason to believe that they included any smuggled goods, only such part of the goods the value of which is equal to the value of the smuggled goods shall be liable to confiscation (Section 120).

(m) Confiscation of sale-proceeds of smuggled goods

Where any smuggled goods are sold by a person having knowledge or reason to believe that the goods are smuggled goods, the sale-proceeds thereof shall be liable to confiscation (Section 121).

7.46 Adjudication of confiscations and penalties

Section 122 provides that in every case in which anything is liable to confiscation or any person is liable to a penalty, such confiscation or penalty may be adjudged:

- (a) without limit, by a Commissioner of Customs or a Joint Commissioner of Customs;
- (b) where the value of the goods liable to confiscation does not exceed two lakh rupees, by an Assistant or Deputy Commissioner of Customs;
- (c) where the value of the goods liable to confiscation does not exceed ten thousand rupees, by a Gazetted Officer of customs lower in rank than an Assistant or Deputy Commissioner of Customs.

(a) Burden of proof in certain cases

Section 123(1), provides that where any goods to which this section applies are seized under this Act in the reasonable belief that they are smuggled goods, the burden of proving that they are not smuggled goods shall be:

- (a) in a case where such seizure is made from the possession of any person:
 - (i) on the person from whose possession the goods were seized; and
 - (ii) if any person, other than the person from whose possession the goods were seized, claims to be the owner thereof, also on such other person;
- (b) in any other case, on the person, if any, who claims to be the owner of the goods so seized.

Section 123 shall apply to gold and manufactures of watches and any other class of goods which the Central Government may by notification in the Official Gazette specify.

The Central Government has notified the following other classes of goods, for the purposes of Section 123(2), namely:

1. Cosmetics.
2. Cigarettes.
3. Transistors and Diodes.
4. Synthetic yarn and Metallised yarn.
5. Fabrics made wholly or mainly of synthetic yarn.

6. Cassette Tape Recorders.
7. Electronic Calculators.
8. Whisky.
9. Watches, watch movements (including partly assembled movements), dials and cases for watches.
10. Zip fasteners.
11. Video Cassette Recorders and Video Cassette Players.
12. T.V. Sets.

(b) Issue of show cause notice before confiscation of goods etc.

Section 124, provides that, no order confiscating any goods or imposing any penalty on any person shall be made under this Chapter unless the owner of the goods or such person:

- (a) is given a notice in writing informing him of the grounds on which it is proposed to confiscate the goods or impose a penalty;
- (b) is given an opportunity of making a representation in writing within such reasonable time as may be specified in the notice against the grounds of confiscation or imposition of penalty mentioned therein; and
- (c) is given a reasonable opportunity of being heard in the matter;

Provided that the notice referred to in clause (a) and the representation referred to in clause (b) may, at the request of the person concerned, be oral.

This provision has been made to make it obligatory on the part of adjudicating officers to follow the principles of natural justice. Any order of confiscation or any order imposing a penalty on any person without giving him an opportunity as laid down in Section 124 becomes void and is set aside in a court of law, as can be seen from the following decrees:

“The Commissioner of Central Excise should see that every show cause notice issued under the provisions of the Act strictly complies with, not only the letter of the law, but also the spirit of it (AIR 1962 MAD. 366 at p. 368). The Department is not absolved of the obligation under Section 124 for issuing a show cause notice before passing an order confiscating any goods or imposing any penalty on any person under Chapter XIV of the Customs Act (AIR 1972 GUJ. 115). The object of the show cause notice is not to merely mention the statutory provisions under which the person to whom the notice is issued is liable to be punished by the imposition of penalty; the real object of such a notice is to indicate, besides the nature of the contravention which is sought to be punished under any provision of the Act, the penalty also that is sought to be imposed on the petitioner (AIR 1962 MAD. 366 at p. 368).

7.47 Option to pay fine in lieu of Confiscation

Under Section 125 whenever confiscation of goods is authorised by this Act, the officer adjudging it may, in the case of any goods, the importation or exportation whereof is prohibited under this Act or any other law for the time being in force, and

shall, in the case of any other goods, give to the owner of the goods, or where such owner is not known, the person from whose possession or custody such goods have been seized, an option to pay in lieu of confiscation such fine as the said officer thinks fit:

Provided that, without prejudice to the provisions of the proviso to Sub-section (2) of Section 115, such fine shall not exceed the market price of the goods confiscated, less in the case of imported goods, the duty chargeable thereon.

Where any fine in lieu of confiscation of goods is imposed the owner of such goods or the other person shall, in addition, be liable to any duty and charges payable in respect of such goods.

On confiscation property to vest in Central Government

- (1) When any goods are confiscated under this Act, such goods shall thereupon vest in the Central Government.
- (2) The officer adjudicating the confiscation shall take and hold possession of the confiscated goods (Section 126).

7.48 Award of confiscation or penalty by customs officers not to interfere with other punishments

The award of any confiscation or penalty under this Act by an officer of Customs shall not prevent the infliction of any punishment to which the person affected thereby is liable under the provisions of Chapter XVI or under any other law (Section 127).

Some important case laws relating to adjudication are given herein below to highlight the parameters within which the adjudicating officer has to function:-

- (a) In revision application of M/s. Bijjee Products (India) Pvt. Ltd., the Government of India observed: "The lower authorities have not gone into the merits of the refund claim nor have they examined whether the claim was within the time limit specified under the Rules. Government of India, accordingly, set aside the order of the Appellate Collector since it is not a speaking order and direct the Appellate Collector to consider the appeal de-novo now and pass an order on merits"- (1982 ELT 591).
- (b) "If a personal hearing was not given to the petitioner at the adjudication/appellate stage in spite of a specific request made by him in reply to the show cause notice, the adjudication order is not sustainable in law.The revision application disposed of without giving a speaking order is also invalid.If the basic order is invalid, the remaining appellate/revisionary orders will also be ineffective". - [1982 ELT 350 (P&H)].
- (c) "If the Collector has disposed of the case in a summary fashion without giving due consideration to the points urged by the Appellants and passing a speaking order dealing with them, the case is fit for remand for de-novo trial." - (1982 ELT 436 CBEC).
- (d) "The Assistant Collector (Adjudicating Officer) has no power under law to modify his earlier order or to issue a corrigendum, for Section 154 of the

Customs Act only provides for the correction of clerical or arithmetical mistakes or any error or errors arising from accidental slip or omission. As such, the corrigendum issued by the Assistant Collector was without authority.” - [1986 (9) ECR 231 - CEGAT].

- (e) “The Assistant Collector, who has given his decision on the 1st February, 1962 has not taken any of these factors into consideration nor has he taken into consideration any of the other evidence offered by the petitioners for deciding this point. Under the circumstances, we find that the decision given by the Assistant Collector, is a result of total non-application of his mind. The same can be said with greater force with regard to the order which the Collector has passed in appeal against the above order. Whatever be the reasons for the Collector to delay his order for months after the appeal was heard, we find that after this long deliberation over the merits of the appeal, the only order which is recorded is: ‘I have examined the facts and merits of the case. I have carefully considered the pleas advanced by the appellants in the appeal petition as also the arguments at the time of personal hearing on 26.12.64. I, however, see no reason to interfere with the decision taken by the Assistant Collector ... in his order ... dated 2.2.63. I uphold the said order and consequently, the appeal is rejected.’ It is too obvious to mention that this order cannot be considered as a speaking order. It does not reveal what the facts are that the Collector took into consideration before coming to his conclusion. Under the circumstances, the order suffers from the same infirmity as the order passed by the Assistant Collector does”. - (1983 ELT 744 GUJ).
- (f) “It is well established that it is not a good return to a rule nisi for the issue of a writ certiorari to state that the order is justified on facts not contained in the order This court cannot take cognizance of any fact which does not appear upon the face of the order. When a statutory functionary makes an order based on certain grounds, its validity must be judged by the reasons so mentioned and cannot be supplemented by fresh reasons in the shape of affidavit or otherwise. Otherwise, an order, bad in the beginning may, by the time it comes to court on account of a challenge, get validated by additional grounds later brought out. This ground is not mentioned in the impugned order”. - 1984 (15) ELT 379 (MAD).
- (g) “.... In this connection, I may state that the Assistant Collector is a quasi-judicial authority and has to discharge his duties and functions in a quasi-judicial manner. I would like to impress upon the Assistant Collector that he is not bound by any administrative instructions. The questions of fact and law which may be raised before him by the parties are required to be determined by him after full application of mind in an objective manner without feeling in any way controlled by any administrative instructions and he will deal with clearly and expressly the reasonings which may be advanced on behalf of the petitioners. It is only when the petitioners’ reasoning is dealt with that it would show that there has been application of mind by him. The above observations have been made in view of the fact that administrative instructions have been brought to my notice by the counsel for the petitioners. For these reasons, the order of the Assistant

Collector and the consequent demands are liable to be quashed". - [1985 (22) ELT 726 (RAJ)].

Special provisions exempting additional duty of customs on import of foreign-going vessels into India (Section 129)

For the period starting 17th March, 2012, full exemption from additional duty has been provided to "foreign-going vessels" imported into India but on the fulfillment of certain conditions viz. that a Bill of entry shall be filed for the vessel when it converts into a "coastal" vessel and additional duty would be payable on the following basis:

- (i) if the licence obtained for coastal trade at the time of conversion is a general one i.e. without specified period of validity, duty would be payable as if there were no exemption;
- (ii) if the licence for coastal trade is for a specified period, and
 - (a) import is by the owner of the vessel or his agent, then 1/120th part of the aggregate duty would be payable on the vessel for each month (or part thereof) of stay in India as a coastal vessel; or
 - (b) if the import is against a lease agreement/ contract, then duty shall be payable on the lease value of the contract.

Illustration I : If a vessel imported by a Shipping Line ABC Company as a foreign-going vessel converts into a coastal vessel for 6 months and the value of the vessel declared by the importer is ₹ 2 crore, the duty payable would be calculated in the following manner:

$$(2 \times 0.0618) \times 6/120 = ₹ 61,800, \text{ where the rate of duty is } 6.18\%$$

Illustration II : If a vessel is imported by an Indian corporate on lease basis for use after import on payment of a total rental of ₹50 lakh for a period of 3 months, the duty payable would be calculated in the following manner:

$$₹50 \times 0.618 = ₹3.09 \text{ lakh, where the rate of duty is } 6.18\%$$

7.49 Offences and Prosecution Provisions

The Customs Act, 1962 contains the following provisions in regard to offences and prosecutions:-

(a) False declaration, false documents, etc.

Whosoever makes, signs or uses, or causes to be made, signed or used, any declaration, statement or document in the transaction of any business relating to the customs, knowing or having reason to believe that such declaration, statement or document is false in any material particular, shall be punishable with imprisonment for a term which may extend to six months, or with fine, or with both (Section 132).

(b) Obstruction of officer of customs

If any person intentionally obstructs any officer of customs in the exercise of any powers conferred under Act, such person shall be punishable with imprisonment for a term which may extend to six months or with fine, or with both (Section 133).

(c) Refusal to be X-rayed

If any person

- (a) resists or refuses to allow a radiologist to screen or to take X-ray picture of his body in accordance with an order made by a magistrate under Section 103; or
- (b) resists or refuses to allow suitable action being taken on the advice and under the supervision of a registered medical practitioner for bringing out goods liable to confiscation secreted inside his body, as provided in Section 103;

he shall be punishable with imprisonment for a term which may extend to six months, or with fine, or with both (Section 134).

(d) Evasion of duty or prohibitions

- (1) without prejudice to any action that may be taken under the Customs Act, if any person –
 - (a) is in relation to any goods in any way knowingly concerned in mis-declaration of value or in any fraudulent evasion or attempt at evasion of any - duty chargeable thereon or of any prohibition for the time being imposed under this Act or any other law for the time being in force with respect to such goods, or
 - (b) acquires possession of or is in any way concerned in carrying, removing, depositing, harbouring, keeping, concealing, selling or purchasing or in any other manner dealing with any goods which he knows or has reason to believe are liable to confiscation under Section 111 or Section 113, as the case may be, or
 - * (c) attempts to export any goods which he knows or has reason to believe are liable to confiscation under Section 113.

he shall be punishable, -

- (i) in the case of an offence relating to any of the goods to which Section 123 applies and the market price whereof exceeds one lakh of rupees, with imprisonment for a term which may extend to (seven years) and with fine:

Provided that in the absence of special and adequate reasons to the contrary to be recorded in the judgment of the Court, such imprisonment shall not be for less than three years;
 - (ii) in any other case, with imprisonment for a term which may extend to three years or with fine, or with both.
- (2) If any person convicted of an offence under this section or under Sub-section (1) of Section 136 is again convicted of an offence under this section, then he shall be punishable for the second and for every subsequent offence with imprisonment for a term which may extend to seven years and with fine:

Provided that in the absence of special and adequate reasons to the

contrary to be recorded in the judgement of the court such imprisonment shall not be for less than one year.

- (3) For the purposes of the above provisions the following shall not be considered as special and adequate reasons for awarding a sentence of imprisonment for a term of less than (one year) namely:-
- (i) the fact that the accused has been convicted for the first time for an offence under this Act;
 - (ii) the fact that in any proceeding under this Act, other than a prosecution, the accused has been ordered to pay a penalty or the goods which are the subject matter of such proceedings have been ordered to be confiscated or any other action has been taken against him for the same act which constitutes the offence;
 - (iii) the fact that the accused was not the principal offender and was acting merely as a carrier of goods or otherwise was a secondary party to the commission of the offence;
 - (iv) the age of the accused.

(e) Preparation

If a person makes preparation to export any goods in contravention of the provisions of the Act, and from the circumstances of the case it may be reasonably inferred that if not prevented by circumstances independent of his will, he is determined to carry out his intention to commit the offence, he shall be punishable with imprisonment for a term which may extend to three years, or with fine, or with both (Section 135A).

(f) Power of court to publish name, place of business, etc., of persons convicted under the Act

(1) Where any person is convicted under this Act for contravention of any of the provisions thereof, it shall be competent for the court convicting, the person to cause the name and place of business or residence of such person, nature of the contravention, the fact that the person has been so convicted and such other particulars as the court may consider to be appropriate in the circumstances of the case, to be published at the expense of such person in such newspapers or in such manner as the court may direct.

(2) No publication under Sub-section (1) shall be made until the period for preferring an appeal against the orders of the court has expired without any appeal having been preferred, or such an appeal having been preferred, has been disposed of.

(3) The expenses of any publication under Sub-section (1) shall be recoverable from the convicted person as if it were a fine imposed by the court (Section 135B).

(g) Offences by officers of customs

(1) If any officer of customs enters into or acquiesces in any agreement to do, abstains from doing, permits, conceals or connives at any act or thing whereby any fraudulent export is effected or any duty of customs leviable on any goods, or any

prohibition for the time being in force under this Act or any other law for the time being in force with respect to any goods is or may be evaded, he shall be punishable with imprisonment for a term which may extend to three years or with fine, or with both.

- (2) If any officer of customs
- (a) requires any person to be searched for goods liable to confiscation or any document relating thereto, without having reason to believe that he has such goods or documents secreted about this person; or
 - (b) arrests any person without having reason to believe that he has been guilty of an offence punishable under Section 135; or
 - (c) searches or authorises any other officer of customs to search any place without having reason to believe that any goods, documents or things of the nature referred to in Section 105 are secreted in that place,

he shall be punishable with imprisonment for a term which may extend to six months, or with fine which may extend to one thousand rupees, or with both.

(3) If any officer of customs, except in the discharge in good faith of his duty as such officer or in compliance with any requisition made under any law for the time being in force, discloses any particulars learnt by him in his official capacity in respect of any goods, he shall be punishable with imprisonment for a term which may extend to six months, or with fine which may extend to one thousand rupees or with both (Section 136).

(h) Cognizance of offences

(1) No court shall take cognizance of any offence under Section 132, Section 133, Section 134 or Section 135, except with the previous sanction of the Commissioner of Customs.

- (2) No court shall take cognizance of any offence under Section 136
- (a) where the offence is alleged to have been committed by an officer of customs not lower in rank than Assistant Commissioner of Customs, except with the previous sanction of the Central Government;
 - (b) where the offence is alleged to have been committed by an officer of customs lower in rank than Assistant or Deputy Commissioner of Customs, except with the previous sanction of the Commissioner of Customs (Section 137).

(3) Any offence under this Chapter may, either before or after the institution of prosecution, be compounded by the Chief Commissioner of Customs on payment, by the person accused of offence to the Central Government, of such compounding amount and in such manner of compounding as may be specified by rules.

Provided that nothing contained in this sub-section shall apply to –

- (a) a person who has been allowed to compound once in respect of any offence under Section 135 and 135A;
- (b) a person who has been accused of committing an offence under this Act which is also an offence under any of the following Acts, namely –
 - (i) the Narcotic Drugs and Psychotropic Substances Act, 1985;

- (ii) the Chemical Weapons Convention Act, 2000;
- (iii) the Arms Act, 1959;
- (iv) the Wild Life(Protection) Act, 1972
- (c) a person involved in smuggling of goods certain specified goods
- (d) a person who has been allowed to compound once in respect of any offence under this chapter for goods of value exceeding rupees one crore;
- (e) a person who has been convicted under this Act on or after the 30th day of December, 2005.

(i) Offences to be tried summarily

Notwithstanding anything contained in the Code of Criminal Procedure, 1973, an offence under this Chapter (other than the offence punishable for a term of imprisonment of three years or more under section 135) may be tried summarily by a Magistrate (Section 138).

(j) Presumption of culpable mental state

(1) In any prosecution for an offence under this Act which requires a culpable mental state on the part of the accused, the court shall presume the existence of such mental state but it shall be a defence for the accused to prove the fact that he had no such mental state with respect to the act charged as an offence in that prosecution.

Explanation — In this section, “culpable mental state” includes intention, motive, knowledge of a fact and belief in, or reason to believe, a fact.

(2) For the purposes of this section, a fact is said to be proved only when the court believes it to exist beyond reasonable doubt and not merely when its existence is established by a preponderance of probability (Section 138A).

(k) Relevancy of statements under certain circumstances

(1) A statement made and signed by a person before any gazetted officer of customs during the course of any inquiry or proceeding under this Act shall be relevant, for the purpose of proving, in any prosecution for an offence under this Act, the truth of the facts which it contains, -

- (a) when the person who made the statement is dead or cannot be found, or is incapable of giving evidence, or is kept out of the way by the adverse party, or whose presence cannot be obtained without an amount of delay or expense which, under the circumstances of the case, the court considers unreasonable; or
- (b) when the person who made the statement is examined as a witness in the case before the court and the court is of opinion that, having regard to the circumstances of the case, statement should be admitted in evidence in the interests of justice.

(2) The provisions of Sub-section (1) shall, so far as may be, apply in relation to any proceeding under this Act, other than a proceeding before a court, as they apply in relation to a proceeding before a court (Section 138B).

(l) Admissibility of micro films, facsimile copies of documents and computers printouts as documents and as evidence

Section 138C authorises the admissibility of (a) microfilms of documents for the reproduction of image(s) embodied in such microfilms; (b) a facsimile copy of a document; and (c) a computer print-out as admissible evidence in any proceedings under the Customs Law without further requirement of production of the original document itself.

Such acceptance is subject to a series of conditions to safeguard revenue interests, whereby the proper officer is allowed to satisfy himself that such print-outs, facimiles or micro films do indeed reflect correctly the position as obtained in the original document itself.

(m) Presumption as to documents in certain cases

Where any document —

- (i) is produced by any person or has been seized from the custody or control of any person, in either case, under this Act or under any other law, or
- (ii) has been received from any place outside India in the course of investigation of any offence alleged to have been committed by any person under this Act,

and such document is tendered by the prosecution in evidence against him and any other person who is tried jointly with him, the court shall —

- (a) presume, unless the contrary is proved, that the signature and every other part of such document which purports to be in the handwriting of any particular person or which the court may reasonably assume to have been signed by, or to be in the handwriting of, any particular person, is in that person's handwriting, and in the case of a document executed or attested, that it was executed or attested by the person by whom it purports to have been so executed or attested;
- (b) admit the document in evidence, notwithstanding that it is not duly stamped, if such document is otherwise admissible in evidence;
- (c) in a case falling under clause (i) also presume, unless the contrary is proved, the truth of the contents of such document.

Explanation - For the purposes of this section, "document" includes inventories, photographs and lists certified by a Magistrate under Sub-section(1C) of Section 110 (Section 139).

(n) Offences by companies

(1) If the person committing an offence under this Chapter is a company, every person who, at the time the offence was committed was in charge of, and was responsible to, the company for the conduct of the business of the company as well as the company, shall be deemed to be guilty of the offence and shall be liable to be proceeded against and punished accordingly:

Provided that nothing contained in this sub-section shall render any such person liable to such punishment provided in this Chapter if he proves that the offence was committed without his knowledge or that he exercised all due diligence to prevent the commission of such offence.

(2) Notwithstanding anything contained in Sub-section (1), where an offence under this Chapter has been committed by a company and it is proved that the offence has been committed with the consent or connivance of, or is attributable to any negligence on the part of, any director, manager, secretary or other officer of the company, such director, manager, secretary or other officer should be deemed to be guilty of that offence and shall be liable to be proceeded against and punished accordingly.

Explanation - For the purposes of this section, —

- (a) “company” means a body corporate and includes a firm or other association of individuals; and
- (b) “director”, in relation to a firm, means a partner in the firm (Section 140).

(o) Application of Section 562 of the Code of Criminal Procedure, 1898, and of the Probation of Offenders Act, 1958

(1) Nothing contained in Section 562 of the Code of Criminal Procedure, 1898 (5 of 1898), or in the Probation of Offenders Act, 1958 (20 of 1958), shall apply to a person convicted of an offence under the Customs Act unless that person is under eighteen years of age.

(2) The provisions of Sub-section (1) shall have effect notwithstanding anything contained in Sub-section (3) of Section 135 (Section 140A).

7.50 Miscellaneous Provisions

The following further provisions in the Customs Act are worth nothing:

(a) Conveyances and goods in a customs area subject to control of officers of customs

All conveyances and goods in a customs area shall, for the purpose of enforcing the provisions of this Act, be subject to the control of officers of customs [Section 141]. In Bombay and Calcutta licensing of boats has been done by notifications issued as far back as in 1908, 1927 and 1950.

(b) Recovery of sums due to Government

(1) Where any sum payable by any person under this Act including the amount required to be paid to the credit of the Central Government under Section 28B, is not paid:

- (a) The proper officer may deduct or may require any other officer of customs to deduct the amount so payable from any money owing to such person which may be under the control of the proper officer or such other officer of customs; or
- (b) The Assistant or Deputy Commissioner of Customs may recover or may require any other officer of customs to recover the amount so payable by detaining and selling any goods belonging to such person which are under

the control of the Assistant or Deputy Commissioner of Customs or such other officer of customs; or

- (c) If the amount cannot be recovered from such person in the manner provided in clause (a) or clause (b):
- (i) the Assistant or Deputy Commissioner of Customs may prepare a certificate signed by him specifying the amount due from such person and send it to the Collector of the district in which such person owns any property or resides or carries on his business and the said Collector on receipt of such certificate shall proceed to recover from such person the amount specified thereunder as if it were an arrear of land revenue, or
 - (ii) the proper officer may, on an authorisation by a Commissioner of Customs and in accordance with the rules made in this behalf, distrain any movable or immovable property belonging to or under the control of such person, and detain the same until the amount payable is paid; and in case, any part of the said amount payable or of the cost of the distress or keeping of the property remains unpaid for a period of thirty days next after any such distress, may cause the said property to be sold and with the proceeds of such sale, may satisfy the amount payable and the cost including cost of sale remaining unpaid and shall render the surplus, if any to such person.

(2) Where the terms of any bond or other instrument executed under this Act or any rules or regulations made thereunder provide that any amount due under such instrument may be recovered in the manner laid down in Sub-section (1), the amount may, without prejudice to any other mode of recovery, be recovered in accordance with the provisions of that Sub-section (Section 142).

(c) Liability under act to be first charge (Section 142A)

As per the provisions of Section 142A any sum payable by an assessee or any other person under this act shall have first charge on the property of the assessee or the person, as the case may be. However amount payable under the following act shall have preference—

- (1) Section 529A of the Companies Act, 1956,
- (2) The Recovery of debts due to Banks and the Financial Institutions Act, 1993,
- (3) The Securitisation and Reconstruction of financial assets and the Enforcement of Security Interest Act, 2002.

(d) Power to allow import or export on execution of bonds in certain cases

(1) Where under the Customs Act or any other law requires anything to be done before a person can import or export any goods or clear any goods from the control of the officers of customs and the Assistant or Deputy Commissioner of Customs is satisfied that having regard to the circumstances of the case. such thing cannot be done before such import, export or clearance without detriment to that person, the

Assistant or Deputy Commissioner of Customs may, notwithstanding anything contained in this Act or such other law, grant leave for such import, export or clearance on the person executing a bond in such amount, with such surety or security and subject to such conditions as the Assistant or Deputy Commissioner of Customs approves for the doing of that thing within such time after the import, export or clearance, as may be specified in that bond.

(2) If the thing is done within the time specified in the bond, the Assistant or Deputy Commissioner of Customs shall cancel the bond as discharged in full and shall, on demand, deliver it so cancelled, to the person who has executed or who is entitled to receive it; and in such a case that person shall not be liable to any penalty provided in this Act or, as the case may be, in such other law for the contravention of the provisions thereof relating to the doing of that thing.

(3) If the thing is not done within the time specified in the bond, the Assistant or Deputy Commissioner of Customs shall, without prejudice to any other action that may be taken under this Act or any other law for the time being in force, be entitled to proceed upon the bond in accordance with law (Section 143).

(e) Duty deferment

(1) When any material is imported under an import licence belonging to the category of Advance Licence granted under the Imports and Exports (Control) Act, 1947 (18 of 1947) subject to an obligation to export the goods as are specified in the said licence within the period specified therein, the Assistant or Deputy Commissioner of Customs may, notwithstanding anything contained in this Act, permit clearance of such material without payment of duty leviable therein.

The permission for clearance without payment of duty under Sub-section (1) shall be subject to the following conditions, that is to say —

- (a) the duty payable on the material imported shall be adjusted against the drawback of duty payable under this Act or under any other law for the time being in force on the export of goods specified in the said Advance Licence; and
- (b) where the duty is not so adjusted either for the reason that the goods are not exported within the period specified in the said Advance Licence, or within such extended period not exceeding six months as the Assistant or Deputy Commissioner of Customs may, on sufficient cause being shown, allow, or for any other sufficient reason, the importer shall, notwithstanding anything contained in Section 28, be liable to pay the amount of duty not so adjusted together with simple interest thereon at the rate of twelve per cent per annum from the date the said permission for clearance is given to the date of payment.

(3) While permitting clearance under the Sub-section (1), the Assistant or Deputy Commissioner of Customs may require the importer to execute a bond with such surety or security as he thinks fit, for complying with the conditions specified in Sub-section (2) (Section 143A).

(f) Power to take samples

(1) The proper officer may, on the entry of clearance or any goods or at any time while such goods are being passed through the customs area, take samples of such goods in the presence of the owner thereof, for examination or testing, or for ascertaining the value thereof, or for any other purposes of this Act.

(2) After the purpose for which a sample was taken is carried out, such sample shall, if practicable, be restored to the owner, but if the owner fails to take delivery of the sample within three months of the date on which the sample was taken, it may be disposed of in such manner as the Commissioner of Customs may direct.

(3) No duty shall be chargeable on any sample of goods taken under this section which is consumed or destroyed during the course of any test or examination thereof, if such duty amounts to five rupees or more (Section 144).

(g) Owner, etc., to perform operations incidental to compliance with Customs Law

All operations necessary for making any goods available for examinations by the proper officer or for facilitating such examination shall be performed by, or at the expense of, the owner, importer or exporter of the goods, as the case may be (Section 145).

(h) Customs house agents to be licensed

(1) No person shall carry on business as an agent relating to the entry or departure of a conveyance or the import or export of goods at any customs station unless such person holds a licence granted in this behalf in accordance with the regulations.

(2) The Board may make regulations for the purpose of carrying out the provisions of this section and, in particular, such regulations may provide for -

- (a) the authority by which a licence may be granted under this section and the period of validity of any such licence;
- (b) the form of the licence and the fees payable therefor;
- (c) the qualifications of persons who may apply for a licence and the qualifications of persons to be employed by a licensee to assist him in his work as an agent;
- (d) the restrictions and conditions (including the furnishing of security by the licensee) subject to which a licence may be granted;
- (e) the circumstances in which a licence may be suspended or revoked; and
- (f) the appeals, if any, against an order of suspension or revocation of a licence and the period within which such appeals shall be filed (Section 146).
Customs House Agents licensing Regulations, 1984 have been framed in exercise of powers conferred under the section.

(i) Appearance by authorised representative

(1) Any person who is entitled or required to appear before an officer of customs or the Appellate Tribunal in connection with any proceedings under this Act,

otherwise than when required under Section 108 to attend personally for examination on oath or affirmation, may, subject to the other provisions of this section, appear by an authorised representative.

(2) For the purposes of this section, "authorised representative" means a person authorised by the person referred to in Sub-section (1) to appear on his behalf, being—

- (a) his relative or regular employee; or
- (b) a customs house agent licenced under Section 146; or
- (c) any legal practitioner who is entitled to practice in any civil court in India; or
- (d) any person who has acquired such qualifications as the Central Government may specify by rules made in this behalf.

(3) Notwithstanding anything contained in this section, no person who was a member of the Indian Customs and Central Excise Service-Group A and has retired or resigned from such Service after having served for not less than three years in any capacity in that service shall be entitled to appear as an authorised representative in any proceedings before an officer of customs for a period of two years from the date of his retirement or resignation, as the case may be.

(4) No person —

- (a) who has been dismissed or removed from the Government service; or
- (b) who is convicted of an offence connected with any proceeding under this Act, the Central Excise Act, 1944 (1 of 1944), or the Gold (Control) Act, 1968 (45 of 1968); or
- (c) who has become an insolvent,

shall be qualified to represent any person under Sub-section (1) for all times in the case of a person referred to in clause (a), and for such time as the Commissioner of Customs or the competent authority under the Central Excise Act, 1944, or the Gold (Control) Act, 1968, as the case may be, may, by order, determine in the case of a person referred to in clause (b), and for the period during which the insolvency continues in the case of a person referred to in clause (c).

(5) If any person,

- (a) who is a legal practitioner, is found guilty of misconduct in his professional capacity by any authority entitled to institute proceedings against him, an order passed by that authority shall have effect in relation to his right to appear before an officer of customs or the Appellate Tribunal as it has in relation to his right to practise as a legal practitioner;
- (b) who is not a legal practitioner, is found guilty of misconduct in connection with any proceedings under this Act by such authority as may be specified by rules made in this behalf, that authority may direct that he shall henceforth be disqualified to represent any person under Sub-section(1).

(6) Any order or direction under clause(b) of Sub-section(4) or clause (b) of Sub-section (5) shall be subject to the following conditions, namely:-

- (a) no such order or direction shall be made in respect of any person unless he has been given a reasonable opportunity of being heard;
- (b) any person against whom any such order or direction is made may, within one month of the making of the order or direction, appeal to the Board to have the order or direction cancelled; and
- (c) no such order or direction shall take effect until the expiration of one month from the making thereof, or, where an appeal has been preferred, until the disposal of the appeal (Section 146A).

(j) Liability of principal and agent

(1) Where the Customs Act requires anything to be done by the owner, importer or exporter of any goods, it may be done on his behalf by his agent.

(2) Any such thing done by an agent of the owner, importer or exporter of any goods shall, unless the contrary is proved, be deemed to have been done with the knowledge and consent of such owner, importer or exporter, so that in any proceedings under this Act, the owner, importer or exporter of the goods shall also be liable as if the thing had been done by himself.

(3) When any person is expressly or impliedly authorised by the owner, importer or exporter of any goods to be his agent in respect of such goods for all or any of the purposes of this Act, such person shall, without prejudice to the liability of the owner, importer or exporter, be deemed to be the owner, importer or exporter of such goods for such purposes:

Provided that where any duty is levied or is short-levied or erroneously refunded on account of any reason other than any wilful act, negligence or default of the agent, such duty shall not be recovered from the agent unless in the opinion of the Assistant or Deputy Commissioner of Customs the same cannot be recovered from the owner, importer or exporter (Section 147).

(k) Liability of agent appointed by the person in charge of a conveyance

(1) Where the customs Act requires anything to be done by the person in charge of a conveyance, it may be done on his behalf by his agent.

(2) An agent appointed by the person in charge of a conveyance and any person who represents himself to any officer of customs as an agent of any such person in charge, and is accepted as such by that officer, shall be liable for the fulfilment in respect of the matter in question of all obligations imposed on such person in charge by or under this Act, or any law for the time being in force, and to penalties and confiscations which may be incurred in respect of that matter (Section 148).

(l) Amendment of documents

Save as otherwise provided in Sections 30 and 41 of the Customs Act, the proper officer may, in his discretion, authorise any document, after it has been presented in the customs house to be amended:

Provided that no amendment of a bill of entry or a shipping bill or bill of export shall be so authorised to be amended after the imported goods have been cleared for home consumption or deposited in a warehouse, or the export goods have been exported, except on the basis of documentary evidence which was in existence at the time the goods were cleared, deposited or exported, as the case may be (Section 149).

(m) Procedure for sale of goods and application of sale-proceeds

(1) Where any goods not being confiscated goods are to be sold under any provisions of the Customs Act, they shall, after notice to the owner thereof, be sold by public auction or by tender or with the consent of the owner in any other manner.

(2) The proceeds of any such sale shall be applied —

- (a) firstly to the payment of the expenses of the sale,
- (b) next to the payment of the freight and other charges, if any, payable in respect of the goods sold, to the carrier, if notice of such things has been given to the person having custody of the goods,
- (c) next to the payment of the duty, if any, on the goods sold,
- (d) next to the payment of the charges in respect of the goods sold due to the person having the custody of the goods,
- (e) next to the payment of any amount due from the owner of the goods to the Central Government under the provisions of this Act or any other law relating to Customs,

and the balance, if any, shall be paid to the owner of the goods (Section 150).

Provided that where it is not possible to pay the balance of sale proceeds, if any, to the owner of the goods within a period of six months from the date of sale of such goods or such further period as the Commissioner of customs may allow, such balance of sale proceeds shall be paid to the central government.

(n) Certain officers required to assist officers of customs

The following officers are empowered and required to assist officers of customs in the execution of this Act, namely:-

- (a) officers of the Central Excise Department;
- (b) officers of the Navy;
- (c) officers of the Police;
- (d) officers of the Central or State Government employed at any port or airport;
- (e) such other officers of the Central or State Governments or a local authority as are specified by the Central Government in this behalf by notification in the Official Gazette (Section 151).

(o) Instructions to officers of Customs

The Board may, if it considers it necessary or expedient so to do for the purpose of uniformity in the classification of goods or with respect to the levy of duty thereon,

or for the implementation of any other provision of this act or of any other law for the time being in force, in so far as they relate to any prohibition, restriction or procedure for import or export of goods issue such orders, instructions and directions to officers of customs as it may deem fit and such officers of customs and all other persons employed in the execution of this Act shall observe and follow such orders, instructions and directions of the Board:

Provided that no such orders, instructions or directions shall be issued -

- (a) so as to require any such officer of customs to make a particular assessment or to dispose of a particular case in a particular manner; or
- (b) so as to interfere with the discretion of the Commissioner of Customs (Appeals) in the exercise of his appellate functions (Section 151A).

(p) Delegation of powers

The Central Government may, by notification in the Official Gazette, direct that subject to such conditions if any, as may be specified in the notification —

- (a) any power exercisable by the Board under this Act shall be exercisable also by a Chief Commissioner of Customs or a Commissioner of Customs empowered in this behalf by the Central Government;
- (b) any power exercisable by a Commissioner of Customs under this Act may be exercised also by a Joint Commissioner of Customs or an Assistant Commissioner of Customs or Deputy Commissioner of Customs empowered in this behalf by the Central Government;
- (c) any power exercisable by a Joint Commissioner of Customs under this Act may be exercisable also by an Assistant Commissioner of Customs or Deputy Commissioner of Customs empowered in this behalf by the Central Government;
- (d) any power exercisable by an Assistant Commissioner of Customs or Deputy Commissioner of Customs under this Act may be exercisable also by a gazetted officer of customs empowered in this behalf by the Board (Section 152).

A number of notifications have been issued under this Section.

(q) Service of order, decision, etc.

Any order or decision passed or any summons or notice issued under the Customs Act, shall be served —

- (a) by tendering the order, decision, summons or notice or sending it by registered post to the person for whom it is intended or to his agent; or
- (b) if the order, decision, summons or notice cannot be served in the manner provided in clause(a), by affixing it on the notice board of the customs house (Section 153).

(r) Correction of clerical errors, etc.

Clerical or arithmetical mistake in any decision or order passed by the Central Government, the Board or any officer of customs under this Act, or errors arising

therein from any accidental slip or emission may, at any time, be corrected by the Central Government, the Board or such officer of customs or the successor in office of such Officer, as the case may be (Section 154).

(s) Rounding off of duty, etc.

The amount of duty, interest, penalty, fine or any other sum payable and the amount of refund, drawback or any other sum due, under the provisions of this Act shall be rounded off to the nearest rupee and, for this purpose, where such amount contains a part of a rupee consisting of paise then, if such part is fifty paise or more, it shall be increased to one rupee and if such part is less than fifty paise it shall be ignored. (Section 154A)

(t) Protection of action taken under the Act

(1) No suit, prosecution or other legal proceeding shall lie against the Central Government or any officer in the Government or a local authority for anything which is done, or intended to be done in good faith, in pursuance of the Customs Act or the rules or regulations.

(2) No proceedings other than a suit shall be commenced against the Central Government or any officer of the Government or a focal authority for anything purporting to be done in pursuance of this Act without giving the Central Government or such officer a month's previous notice in writing of the intended proceeding and of the cause thereof, or after the expiration of three months from the accrual of such cause (Section 155).

(u) General power to make rules

(1) Without prejudice to any power to make rules contained elsewhere in the Customs Act, the Central Government may make rules consistent with this Act generally to carry out the purposes of this Act.

(2) In particular and without prejudice to the generality of the foregoing power, such rules may provide for all or any of the following matters, namely:

- (a) the manner of determining the price of imported goods under Sub-section (1A) of Section 14.
- (b) the conditions subject to which accessories of, and spare parts and maintenance and repairing implements for, any articles shall be chargeable at the same rate of duty as that article;
- (c) omitted by Section 80 of the Finance Act, 1988;
- (d) the detention and confiscation of goods the importation of which is prohibited and the conditions, if any, to be fulfilled before such detention and confiscation and the information, notices and security to be given and the evidence requisite for the purposes of such detention or confiscation and the mode of verification of such evidence;
- (e) the reimbursement by an informant to any public officer of all expenses and damages incurred in respect of any detention of any goods made on his information and of any proceedings consequent on such detention;

- (f) the information required in respect of any goods mentioned in a shipping bill or bill of export which are not exported or which are exported and are afterwards re-landed;
- (g) the publication, subject to such conditions as may be specified therein, of names and other particulars of persons who have been found guilty of contravention of any of the provisions of this Act or the Rules (Section 156),
- (h) the amount to be paid for compounding and the manner of computing under Sub-section (3) of Section 137.

(v) General power to make regulations

(1) Without prejudice to any power to make regulations contained elsewhere in this Act, the Board may make regulations consistent with this Act and the rules, generally to carry out the purposes of this Act.

(2) In particular and without prejudice to the generality of foregoing power, such regulations may provided for all or any of the following matters, namely:

- (a) the form of a bill of entry, shipping bill, bill of export, import manifest, import report, export manifest, export report, bill of transshipment, declaration for transshipment, boat note and bill of coastal goods;
- (ai) the manner of export of goods, relinquishment of title to the goods and abandoning them to customs and destruction or rendering of goods commercially valueless in the presence of the proper officer under clause (d) of sub-section (1) of section 26A;
- (aia) the form and manner of making application for refund of duty under sub-section (2) of section 26A.
- (aa) the Form and manner in which an application for refund shall be made under Section 27;
- (b) the conditions subject to which the transshipment of all or any goods under Sub-section (3) of Section 54, the transportation of all or any goods under Section 56 and the removal of warehoused goods from one warehouse to another under Section 67 may be allowed without payment of duty;
- (c) the conditions subject to which any manufacturing process or other operations may be carried on in a warehouse under Section 65 (Section 157).
- (d) the manner of conducting audit of the assessment of duty of the imported or export goods at the office of the proper officer or premises of the importer or exporter, as the case may be.

(w) Provisions with respect to rules and regulations

(1) All rules and regulations made under this Act shall be published in the Official Gazette.

(2) Any rule or regulation which the Central Government or the Board is empowered to make under this Act may provide:

- (i) for the levy of fees in respect of applications, amendment of documents, furnishing of duplicates of documents, issue of certificates, and supply of statistics, and for rendering of any services by officers of customs under this Act;

- (ii) that any person who contravenes any provision of a rule or regulation or abets such contravention or who fails to comply with any provision of a rule or regulation with which it was his duty to comply, shall be liable to a penalty which may extend to five hundred rupees.

(x) Rules and certain notifications to be laid before Parliament

Every rule or regulation made under this Act, every notification issued under Sections 11, 11 B, 11 H, 11 -I, 11K, 11N, 14, 25, 28A, 43, 66, 69, 70, 74, 75, 76, 98, 98A, 101 and 123 and every order made under Sub-section (2) of Section 25, other than an order relating to goods of strategic, secret, individual or personal nature, shall be laid, as soon as may be after it is made or issued, before each House of Parliament, while it is in session, for a total period of thirty days which may be comprised in one session, or in two or more successive sessions, and if, before the expiry of the session immediately following the session or the successive sessions aforesaid, both Houses agree in making any modification in the rule or regulation or notification or order, or both Houses agree that the rule or regulation should not be made or notification or order should not be issued or made, the rule or regulation or notification or order shall thereafter have effect only in such modified form or be of no effect as the case may be; so, however, that any such modification or annulment shall be without prejudice to the validity of anything previously done under that rule or regulation or notification or order. (Section 159).

(y) Effect of amendment etc. of Rules, Regulations, Notifications or Orders (Section 159A)

Where any rule, regulation, notification or order made or issued under this Act or any notification or order issued under such rule or regulation, is amended, repealed, superseded or rescinded, then, unless a different intention appears, such amendment, repeal, supersession or rescinding shall not:

- (a) Revive anything not in force or existing at the time at which the amendment, repeal, supersession, or rescinding takes effect; or
- (b) affect the previous operation of any rule, regulation, notification or order so amended, repealed, superseded or rescinded or anything duly done or suffered thereunder, or
- (c) affect any right, privilege, obligation or liability acquired, accrued or incurred under any rule, regulation, notification or order so amended, repealed, superseded or rescinded; or
- (d) affect any penalty, forfeiture or punishment incurred in respect of any offence committed under or in violation of any rule, regulation notification or order so amended, repealed, superseded or rescinded; or
- (e) affect any investigation, legal proceeding or remedy in respect of any such right, privilege, obligation, liability, penalty, forfeiture or punishment as aforesaid, and any such investigation, legal proceeding or remedy may be instituted continued or enforced and any such penalty, forfeiture or punishment may be imposed as if the rule, regulation, notification or order, as the case may be, had not been amended, repealed, superseded or rescinded.”

LESSON ROUND UP

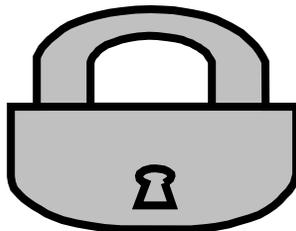


This Chapter includes:

- Introduction
- Taxable Event
- Types of duties under Custom
- Tariff classification
- Valuation of Goods For Levy of Customs Duty
- Customs Valuation (Determination of Price of Imported Goods) Rules, 2007
- Custom Valuation (Determination of Value of Export Goods) Rules, 2007
- Determination of Rate of Duty And Tariff Valuation
- Remission, Exemption and Demands in Customs
 - Duty on Pilfered goods
 - Re-Importation of Goods
 - Goods derelict, wreck, etc.
 - Abatement of duty
 - Remission of duty on lost, destroyed and abandoned goods
 - Exemption from duty
 - Policy guidelines for ad hoc exemption under Section 25(2)
 - Refund of Duties
- Recovery of Duties
- Recovery of duties not levied or short levied or erroneously refunded under Section 28
- Power not to recover duties
- Interest on delayed payment of duty under Section 28AA
- Recovery of duties in certain cases under Section 28AAA
- Assessment of duty (Section 17)
- Provisional Assessment of duty (Section 18)
- Advance Ruling
- Clearance of Imported or Exported Goods Including Baggage
- Assessable Value and Levy of Duty—Method of Assessment
- Clearance of Export Cargo
- Customs procedure – Documentation for Export
- Shipment (Export) under claim for drawback
- Procedure for Exports through inland Container Depots
- Procedure for Exports of Containers and Cargo from Inland Container
- Baggages

- Goods Imported or Exported by Post
- Stores
- Provisions Relating to Coastal Goods and Vessels Carrying Coastal Goods
- Duty Drawback
- Transportation of Goods
- Warehousing
- Adjudication and appellate provisions:
- Powers of Committee of Chief Commissioners of Customs or Commissioners of Customs to pass certain orders (Section 129D)
- Appeal to Supreme Court (Section 130E)
- Deposit, pending appeal, of duty and interest demanded or penalty levied
- Interest on delay payment of Refund (Section 129EE)
- Customs (Appeals) Rules, 1982
- Settlement Commission
- Customs and Central Excise Settlement Commission Procedure, 2007
- Search, Seizure, Arrest, Confiscation Etc.
- Confiscation of Goods
- Adjudication of confiscation and penalties
- Option to pay fine in lieu of confiscation
- Award of confiscation or penalty by Customs Officers not to interfere with other punishments
- Offences and Prosecution Provisions
- Miscellaneous Provisions

SELF-TEST QUESTIONS



1. What is the mechanism provided in the Customs Act for adjudication of disputes between the assessee and the department?
2. When can an appeal be filed before the Commissioner (Appeals)?
3. What is Customs, Excise and Gold (Control) Appellate Tribunal (CEGAT)?
4. What are the matters in respect of which an appeal can be made before CEGAT?
5. What is the procedure of filing and disposal of stay petitions under CEGAT Rules?
6. What are the revisionary powers of the Central Government on adjudicated matters under Customs Act?

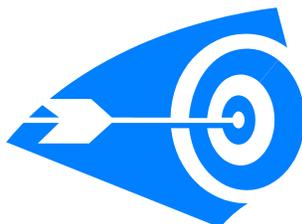
7. When does an appeal lie before Supreme Court under appellate provisions of Customs Act, 1962?
8. What is the procedure of filing a revision application to the Central Government under appellate provisions of Customs Act?
9. Who can act as an 'authorised representative' in adjudication of disputes and appeals under the Customs Act and Rules?
10. Explain briefly the concept of Settlement Commission.
11. What provisions are made under the Customs Act, 1962 to deal with various kinds of offences of Customs?
12. Can a mere preparation towards an act of offence of Customs laws be punished under the Act? State the circumstances.
13. What are the provisions under Customs Act, regarding the power of Court to publish name, place of business, etc. of persons convicted under the Act?
14. When can a Court take cognizance of an offence committed under the Customs Act, 1962?
15. What are the provisions under the Customs Act, with regard to use of Statements, and documents as evidence during prosecution for an offence of Customs?
16. What powers the officers of Customs have in respect of recovery of sums due to the Government on account of duties of Customs?
17. When can an import of material be cleared without payment of duty leviable thereon?
18. State the requirements laid down under the Customs Act with regard to the 'eligibility to function' as an import or export agent.
19. Who is an 'authorised representative' for the purpose of appearance before an officer of Customs or Customs Tribunal.
20. What are the provisions under Customs Act, regarding the search of suspected persons?
21. What are the powers of Customs Officer with regard to search of premises and stoppage and search of conveyance?
22. What are the provisions with regard to confiscation of improperly imported goods and penalty thereon ?
23. When does an exporter is liable for confiscation of goods and penalty thereon as per the provisions of Customs Act, 1962?
24. When does a conveyance used for import or export of goods is liable for confiscation?
25. What is the liability of the owner of the confiscated conveyance and how he can get relieved of the same ?

26. What are the provisions with regard to confiscation of smuggled goods in case such goods are mixed with other goods or are repacked or are changed in form etc. ?
27. What do you understand by the term 'Duty Drawback'?
28. Which kinds of duties paid or payable are allowed to be refunded or rebate allowed, under 'Duty Drawback' scheme?
29. What are the essential elements required for entitlement of 'drawback' on re-export of imported goods?
30. How is 'drawback' determined on export goods manufactured, processed etc, with the use of imported material?
31. What is the relevance of Customs and Central Excise Duties Drawback Rules, in implementation of duty drawback scheme? Are there are any changes made in these rules recently. State briefly.
32. Can the rate or amount of drawback be determined provisionally? State the provisions in this regard.
33. What remedy is provided to the exporter under the rules in case the amount or rate of drawback determined is lower?
34. When are the goods said to be in transit within the meaning of Customs Act, 1962?
35. How are the goods in transit treated for the purpose of levying of duties of customs.
36. When does the officer of Customs may permit the transshipment of goods without payment of duty?
37. What are the conditions laid down under Customs Act, 1962 or any other legislation on the matter with regard to transshipment of goods without payment of duty?
38. How is the term 'Warehouse' defined under Customs Act, 1962?
39. What are 'Public' (Bonded) Warehouses and Private (Bonded) Warehouses?
40. What are the provisions regarding appointment of Public (Bonded) Warehouses and Licensing of Private (Bonded) Warehouses under the Customs Act, 1962?
41. What is the procedure of Re-warehousing of imported goods in Public (Bonded) Warehouses?
42. How Export of goods is essential for the development of an economy?
43. What concessions and incentives have been offered by a Government in order to boost exports?
44. Which main documents are required to be prepared for effecting Export of Goods?
45. What is a 'Shipping Bill'? How it is prepared and used ?

46. What are the kinds of Shipping Bills ?
47. What is 'GR' form and how it is obtained?
48. What is the procedure with regard to obtaining of 'Export Trade Licence'?
49. What are the provisions regarding 'Draw back' of duties on Exported goods under Customs Act, 1962?
50. What is duty 'Draw back'? State the reasons for this allowance.
51. What is the procedure for "claiming duty drawback"?
52. Explain the concept of 'Containerisation' in Import-Export trade and how does it compare with the conventional ships?
53. How the various customs ports, airports and places are fixed for the purpose of loading/unloading of goods subject to levy of duties of Customs?
54. Which organisations are involved in clearance of import Cargo?
55. What is 'Bill of Entry'? What are the different kinds of 'Bill of Entry'?
56. What is the procedure of preparation and filing of 'Bill of Entry'?
57. How are the goods Imported but not cleared by Customs dealt with?
58. How is the assessable value and rate of duty determined under the Customs Act, 1962?
59. What are the provisions in the Customs Act, 1962 with regard to examination of goods before order of clearance?
60. What is "Out of Customs charge" order for delivery of goods?
61. What are the provisions regarding making of "Provisional Assessment" of import duty?
62. What are the provisions regarding clearance of goods imported by post?
63. What specific points one should keep in mind in the clearance of imported cargo for home consumption?
64. What is the object of levying of duties on Import and Export of goods?
65. How is the territorial limits of India fixed for the purpose of Import and Export of goods.
66. What kinds of Import duties are provided under the Customs Act, 1962?
67. How is the 'assessment value' of imported goods determined for the purpose of levying of Import duties under the Customs Act, 1962? Is there any change in the law in this regard in the recent past? Explain.
68. What cost elements constitute the value of imported goods for the purpose of assessable value?
69. What is the concept of 'Transaction Value' introduced through the newly enacted Valuation Rules, 1988?
70. Under what circumstances 'Transaction Value' may not be accepted for valuation of imported goods?
71. How is the custom duty levied in case imported goods are pilfered before clearance?

72. How is the rate of Duty and Tariff Valuation determined in case of imported goods?
 73. How is the rate of duty determined in case of export goods?
 74. What is the procedure of assessment of Customs Duty in case of import and export of goods?
 75. What are the circumstances under which customs duties may be assessed provisionally?
 76. What is the procedure and conditions of provisional assessment of customs duties?
 77. How is the customs duty determined where goods consist of articles liable to different rates of duty?
 78. State the circumstances when the abatement of customs duty may be allowed under the Act?
 79. What are the provisions with regard to levying of duties of customs on goods found derelict, wreck, etc. on importation?
 80. What are the provisions of Customs Act, 1962 with regard to remission of duty on lost, destroyed or abandoned goods?
 81. What are the provisions of Customs Act, 1962 with regard to grant of exemption from custom duty ?
 82. State the circumstances and reasons for providing of exemptions from customs duty under the Customs Act, 1962.
 83. Who has the power to grant exemptions of customs duty and what kinds of exemptions can be granted within the provisions of Customs Act, 1962?
 84. State the circumstances under which refund of export duty is permitted.
 85. When can the claim for refund of customs duty be made and what is the procedure for the same?
 86. What are the provisions under the Customs Act, 1962 regarding recoveries of duties with retrospective effect? State the circumstances and reasons.
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STUDY VIII
PROMISSORY ESTOPPEL IN FISCAL LAWS



LEARNING OBJECTIVES

The objective of the Chapter is to discuss the following topics/concepts :

- Promissory Estoppel in Fiscal Laws
- Customs Act and Tax Planning
- Excise Law and Tax Planning
- CENVAT

8.1 PROMISSORY ESTOPPEL IN FISCAL LAWS

The doctrine of promissory estoppel has its genesis in the law of equity and being closely related to various schemes for allowing tax concessions to certain new industrial units set up within specified time or in specified places, it has become very relevant in fiscal legislations particularly in Sales-tax, Excise and Custom duty disputes. The doctrine is not limited in its application only to defence but also in a cause of action. This concept and its applicability has often been agitated before the court in the context of sales tax exemption. The gist of equity lies in the fact that one party has by his conduct or representation led the other to alter his position. If injustice can be avoided only by enforcement of the promise, it is a case of estoppel.

In *Delhi Cloth and General Mills Ltd. v. Union of India*, it was held that :

“All that is now required is that the party asserting the estoppel must have acted upon the assurance given to him. Must have relied upon the representation made to him. It means, the party has changed or altered the position by relying on the assurance or representation. The alteration of position by the party is the only indispensable requirement of the doctrine. It is not necessary to prove further any damage, detriment or prejudice to the party asserting the estoppel.

The concept of estoppel has been explained in Section 115 of Indian Evidence Act as follows:

When one person has by his declaration, act or omission, intentionally caused or permitted another person to believe a thing to be true and to act upon such belief, neither he nor his representative shall be allowed, in any suit or proceeding between himself and such person or his representative, to deny the truth of the thing.

The doctrine of estoppel has its origin in principles of Equity. It was defined under Section 115 of the Evidence Act, 1872. The estoppel operates as a legal protection to the person who acts in good faith on the basis of express or implied conduct of others and suffers a damage.

8.1.1 DOCTRINE OF PROMISSORY ESTOPPEL UNDER TAX LAWS

This is raised in tax matters, especially in Sales tax where the Government provides exemption from tax by means of tax holiday for a certain period say 5 years and withdraws the exemption before the expiry of 5 years.

The plea of promissory estoppel is on the ground that certain units have been established expecting the tax benefits and the withdrawal before the expiry has caused damage to them. Here, the units might be hit hard. They can go to the court of law against the Govt. under Doctrine of Estoppel. The doctrine was first introduced in *Hughes v. Metropolitan Rly. Co.*, 1877, Appeal case 439. Lord Cairns stated the doctrine in the following words :

“It is the first principle upon which all Courts of Equity proceed, that if parties who have entered into definite and distinct terms involving certain legal results afterwards by their own act or with their own consent enter upon a course of negotiation which has the effect of leading one of the parties to suppose that the strict rights arising under the contract will not be enforced, or will be kept in suspense, or held in abeyance, the person who otherwise might have enforced those rights will not be allowed to enforce them where it would be inequitable having regard to the dealings which have thus taken place between the parties”.

*The doctrine of promissory estoppel is also known as **equitable estoppel or quasi estoppel.***

Courts on Promissory Estoppel

The courts while recognizing the principle of promissory estoppel as an instrument of equity remedy have consistently held that the ‘promissory estoppel plea’ fails where ‘public interest’ intervenes. That means, though a concession is extended for a fixed period by a notification or otherwise the same can be withdrawn in public interest in *Sales Tax Officer & Another v. M/s. Shree Durga Oil Mills* (1997) 7 SCALE, 726, the honourable Supreme Court held that a notification granting exemption of taxes can be withdrawn at any point of time. There can not be estoppel against any statute. Where it is in public interest, the court will not interfere because public interest must override any consideration of private loss or gain.

In *Sree Sales Corporation & Another v. U.O.I.* (1997) 3 SCC 398, it was held that where there was supervening public interest, the Govt. is free to change its stand and withdraw the exemption already granted. Recently, in *Sharma Transport v. Govt. of A.P. & Others* (2002) S.C., the Supreme Court observed “one such reason for changing its policy decision can be resource crunch and the loss of public revenue. There is preponderance of judicial opinion that to invoke the doctrine of promissory estoppel, clear sound and positive foundation must be laid in the petition itself by the party invoking the doctrine and that bold expressions without any supporting material to the effect that the doctrine is attracted because the party invoking the doctrine has altered his position relying on the assurance of the Govt. would not be sufficient to press into aid the doctrine. ‘Doctrine of promissory estoppel’ has been evolved by Courts on the principles of equity, to avoid injustice.

In the above case, the appellants were operators of tourist buses originating from the State of Karnataka and running their buses in adjacent states including the state of A.P.

The vehicles of the appellants were covered by tourist vehicle permits by virtue of which, their vehicles were authorised to ply in certain contiguous states also.

The Central Government formulated policies in the matter of concessions to be extended to tourist vehicles. Based on the directive of the Central Govt. an order was issued on 1st July, 1995 conferring the benefits of a concessional rate of tax to tourist operators. But on 5th June 2000, the State Govt. issued a notification under A.P. Motor Vehicles Taxation Act, 1963 cancelling the earlier order of 1995. The operators after losing the High Court of A.P. filed an appeal before the Supreme Court. The Contentions before the apex Court were — that the directives of the Central Govt. were binding on the State Govt. and that the withdrawal of tax concession is illegal. They also contended that under doctrine of promissory estoppel, a concession extended by the Govt. could not be withdrawn.

But the Supreme Court rejects the pleas and dismissed the appeal stating that the state of A.P. is justified in withdrawing the benefits in public interest. Also held that the doctrine of promissory estoppel is not applicable in the case.

Thus we can conclude that the doctrine of promissory estoppel is a valid proposition but it will be disallowed by courts when the withdrawal of tax benefit by the Govt. is to save the larger interests of the public.

As can be seen from the analysis of the cases above, the concept of Promissory Estoppel has assumed considerable significance in sales tax law. Many a time the State Governments with a view to giving a spur to industrial development in the State give sales tax exemptions. Subsequently, State Governments may either withdraw the exemption notification or introduce certain restrictive covenants. This becomes necessary in view of the loss of the revenue to the State Government, as a result of the sales tax exemption granted earlier. In such a situation, whether the State has to be held bound to the representation made earlier to the trade or not depends upon whether the exemption was for a particular period or whether the industry has altered its position in the light of the notification etc. It is once again reiterated that if a State Government issues a general exemption notification with no reference to any period of time such exemption may be amended or varied at any time. There would be no question of any promissory estoppel in such cases. But where the State Government hold out that exemption from sales tax would accrue for a given period of time of three years or five years than promissory estoppel would be applied.

Tax planning exercise needs to be undertaken with great amount of care and discretion. It should not border on evasion nor should it merely be a device to circumvent the letter of law. **In this context the Supreme Court's Judgements in *Mc Dowel and Company Ltd. v. Commercial Tax Officer* 1985, 5, ECC 259 was also studied in full text.** This judgment signaled a departure from the West Minster Principle upon which most of the tax planning used to be founded and which for long had the judicial blessing. But the winds have changed since and in England the West Minster Principle has been given a go by. The Mc Dowel's judgement is a vindication of judicial attitude currently prevailing in England on the use of certain devices to avoid proper incidence of tax.

A trader or a Business entity need not be complacent in regard to payment of indirect taxes, for the simple reason that these are passed on to the consumers. It would only be a reiteration to say that tax planning is as much relevant and important in indirect taxes as it is in direct taxes.

The approach of tax planning has been to give a very rudimentary idea of tax planning *vis-à-vis* indirect taxes. No attempt has been made to repeat and elaborate discussions on various case laws concerning Excise, Customs and Sales Tax. The presentation is only skeletal and indicative of the broad contours of tax planning.

8.2 CUSTOMS ACT AND TAX PLANNING

Customs Act concerns Import and Export of Goods and restrictions and regulations relating thereto. Every importer or exporter and every buyer from such importer for instance, are interested in customs duty planning. For an importer, the tax planning centers round the classification of import goods and valuation of those goods. Improper classification of goods may lead to higher incidence of Customs Duty. On the other hand, even a proper and appropriate classification may not be a ground for feeling relaxed. Because even after correct classification, the valuation of Import of goods may be high pitched with the result the absolute incidence of customs duty would be much more than what it ought to have been. Importers therefore have to pay special attention to problems of classification and valuation of imported goods.

As regards valuation under the Customs law, besides the statutory provisions there are Customs Valuation Rules also. Apart from these, a good amount of case law has developed on what items are to be added to the value of the goods and what items go to reduce the value of goods. A proper tax planning exercise would have to take into consideration these aspects.

(a) Customs Act and Classification of goods

Classification of imported goods is very significant because a wrong classification may lead to a very high incidence of Customs Duty. The importer has therefore to be fully convergent with principles of classification of goods.

Since the subject of taxation is "goods", the concept underlying the levy is required to be understood. It is not the personal opinion of an individual Officer or for that matter of the assessee with regard to the classification of the "goods", that governs the issue. There are certain well defined criteria laid down by judicial decisions, which are required to be kept in mind. We saw what happened in the fountain pens case. In the case of *V.V. Iyer v. Jasjit Singh* (AIR 1973 SC 194), the appellant, who carried on business of importing plantation and agricultural machinery and implements had imported certain parts of agricultural machinery known as express Battery Sprayers which were classified under SL. No: 74 (x) of Part V of the Import Tariff Schedule which related to "sprayers (other than power driven) and parts". The appellant's contention was that he held an import licence for import of goods falling under serial No. 74(vi) of the said part of the said Schedule which related to "Parts of power driven agricultural machinery", the goods imported (liquid containers) were parts of sprayers and the said serial no. 74(vi), permitted all kinds of spare parts of power driven agricultural machinery. The sprayers imported, according

to the appellant, function normally with the help of power driven pumps and functionally, therefore, what the appellant imported were, correctly falling within serial No. 74(vi). As discussed earlier, the Supreme Court, however, did not interfere with the conclusions arrived at by the customs authorities.

In doing so, the Supreme Court was reiterating its earlier decisions in *Collector of Customs, Madras v. K. Ganga Shetty* [AIR (1963) SC 1319], and *A.V. Venkateswaran v. A.S. Wadhvani*, (AIR (1961) SC 1506), In Ganga Shetty's case, the respondent had imported from Australia a quantity of oats which was described in the indent, contract and shipping documents as "standard feed -oats". The commodity imported consisted of oats in whole grain. The question related to the proper classification of goods. The controversy centered round the point whether the "feed - oats" fell within S.No. 42 or S.No. 32 of the relevant Import Trade Control Schedule. During the relevant period S.No. 42 read:

"Fodder, bran and pollards, for the import of which a Special import licence was necessary" while item 32 read:

"Grain, not elsewhere specified, including broken grain but excluding flour -

- (a) oats;
- (b) others;

for which a licence was required.

The customs department held that the goods fell under S. No. 32 and established a case of importation without a valid licence. The contention of the importer was that the "feed oats" fell under the item relating to "fodder" because he had imported the goods solely for feeding race horse, at Bangalore and in South India, oats was not used as human food but only as a feed for horses and in any case, he was misled regarding the correct classification by an affirmative answer he had received from the Deputy Chief Controller of Imports, Madras to whom he had made a reference as to whether the goods could be imported under O.G.L. In the High Court, the decision was in favour of the respondent on the ground that in the Court's view, that "oats" fell under item 42 relating to "fodder" and that the decision of lower authorities was always open for judicial review.

In appeal the Supreme Court however, held that the High Court was not right in interfering with the decision of the Customs authorities since their decision to treat it as falling under item 32 "could not be said to be a view on which no reasonable interpretation could be entertained". In other words, the Supreme Court felt that the 'conclusion or decision of the customs authorities was rationally supportable".

A classic decision which helps resolve classification disputes is found in the decision of the Supreme Court, in the case of *Union of India v. Delhi Cloth and General Mills* [AIR (1963) SC 791]. Although, the case relates to classification of goods, for excise duty purposes it has great significance to the subject matter of discussion as it lays down the philosophy underlying classification of goods. In that case, the respondents were manufacturers of vegetable products known as vanaspati. In the course of manufacture of this product, they were purchasing from the open market groundnut and til oil and subjecting them to different processes

before applying the process of hydrogenation which was essential for making vanaspati. The excise authorities wanted to tax this oil at this intermediary state, under tariff item 23 of the Central Excise Tariff (as it then was) as "refined oil, "all sorts, in or in relation to the manufacture of which any process is ordinarily carried on with the aid of power". The Supreme Court held that excise duty being a tax on manufactured goods and not on their sale, the respondents would no doubt be liable to duty if they produced "refined oil" as "known in the market" at an intermediary stage and since there could be no refined oil as known in the market without the process of deodrisation, they could not be said to have produced "refined oil" as sought by the taxing authorities.

In *South Bihar Sugar Mills v. Union of India* [AIR (1968) SC 922] again, another case of excise classification further illustrates the point. There, the appellants were manufacturing sugar by carbonation process and paid duty on sugar under the relevant tariff item (item No, 1 of the Central Excise Tariff as it then was. For the purpose of this carbonation process, the mills had produced a gas known as "Kiln gas" which besides containing carbon dioxide, also contained other impurities like nitrogen, oxygen and a small quantity of carbon monoxide. According to the excise authorities this "kiln gas" attracted duty under the relevant tariff items (item No. 14(iv) of the Central Excise Tariff as it then was, relating to "compressed liquified or solidified gases including carbonic acid (carbon dioxide). The manufacturers on the other hand disputed this claim on the ground that what they generated was not carbon dioxide as was known to the market and that it was impure gas, containing, besides carbon dioxide certain other impurities too, which was not the case with carbon dioxide available in the market.

Applying the ratio of its earlier decision in the DCM'S case above referred to, the Supreme Court held that the "mixture of gases produced from the Kiln" was known both in the trade and Science as 'Kiln gas' and not as carbon dioxide and hence not liable to duty as contended by the excise authorities.

The Supreme Court observed that the Act, charged duty on manufacture of goods. The word "Manufacture" implies a change but every change in the raw material is not "manufacture". There must be such a transformation that a "new and different" article must emerge having a distinctive name, character and use. The Court observed:

"The duty is levied on goods. As the Act does not define goods, the legislature must be deemed to have used that word in its ordinary dictionary meaning. The dictionary meaning is that to become goods, it must be something which is known to the market".

In *Ramavtar Budriprasad v. Assistant Sales Tax Officer* [AIR (1961) SC 1325], the question before the Supreme Court was whether "betal leaves" could fall within the category of "vegetables" for purposes of assessment to sales tax and the court held that the latter could not include within its scope the former, since both were two distinct and separate commodities. The Court held that since the said expressions were not defined by the statute (C.P. and Berar Sales Tax Act 1947 as amended by the C.P. and Berar Act of 1948), and being a word of "every day" use, it must be construed in its proper sense, meaning "that sense in which people conversant with the subject matter with which the statute is dealing would attribute to it.

In *Commissioner of Sales Tax, Madhya Pradesh v. Jaswant Singh*, the Supreme Court further explained the basis for classification of goods. The question before the Court was whether “charcoal” was included in “coal” for assessment of sales tax. It was held that the Sales Tax Act being one levying a tax on goods must, in the absence of a technical term or a term of science or art, be presumed “to have used an ordinary term as coal according to the meaning ascribed to it in “common parlance”. Viewed from this point, the Court held that both a merchant dealing in coal and a consumer wanting to purchase it would regard coal not in its geological sense but in the sense as “ordinarily understood” and would therefore include charcoal in the term “coal”.

In *Annapurna Carbon Industries v. State of Andhra Pradesh* [AIR (1975) SC 1418] the Supreme Court laid down the test of “predominant” or “ordinary purpose” as deciding factors for determination of classification of goods. It was not the exceptional use or extraordinary use to which the goods could be put to but how predominantly it was used. The Supreme Court further laid down that the fact that the article could be put to any other use also would not detract from the position explained and that the test of general or predominant user was the true test in such matters.

From the above discussion it is clear that while classifying goods for duty purposes due regard should be had to the above principles and it is open for the importer to help the correct classification by establishing how the commodity was popularly known in the particular trade or business in connection with which the goods imported would be used.

In *Commissioner of Sales Tax Madhya Pradesh v. Bhaket Rai* (19 Sales Tax Cases, 285) the Madhya Pradesh High Court, considered the question whether coconuts, groundnut kernel and jira were oil seeds attracting duty under the relevant tariff item (Item 3 of Part II of Schedule I) of the Madhya Pradesh General Sales Tax Act, 1958. The Sales Tax Tribunal had taken the view that these articles were oil seeds in as much as they were seeds and oil could be extracted from them. On reference the High Court took the view that the term oil “seeds” not having been defined by the statute, should be construed in that sense which “people conversant with the subject matter with which the statute was dealing would attribute to it.” Those articles, in the opinion of the Court, were not known as “oil seeds” in common parlance used principally for the extraction of oil and therefore, could not attract the tax.

The Punjab High Court in *Kanpur Textile Finishing Mills case* [AIR (1956) Punjab 130] laid down that:

When dealing with a particular business or transaction words are presumed to have been used with the particular meaning with which they are used and understood in the particular business.”

In *National Hurricane Works v. Union of India* [AIR (1967) Delhi 156], the Delhi High Court dealing with the Import Tariff laid down that if a particular term or word has not been defined in the tariff, then one has to go by the ordinary meaning of the term and that if an item falls specifically under one entry, it cannot by the “process of stretching be brought to fall under another entry”.

It is a settled legal position that if words or expressions used in the tariff are not defined in the body of the statute or the tariff then, regard shall be had to technical opinions, dictionaries and treatises on the subject, including ISI standards.

The basic principle underlying adjudication is to act judicially and not arbitrarily.

The Supreme Court has categorically laid down in *G. Nageshwara v. A.P.S.R.T. Corporation* (AIR) (1959) SC 308, that rules of natural justice require that quasi judicial authorities empowered to decide any dispute must decide the cases without any bias on the principle that "justice should not only be done, but also should manifestly and undoubtedly be seen to be done."

In *Shri Baidyanath Ayurved Bhawan Ltd. v. Asstt. Collector of Central Excise, Allahabad*, the Allahabad High Court was perturbed that even though the collector (appeals) had directed de-novo adjudication of the case, a personal hearing was not granted by the Adjudicating authority (even though a specific request in this behalf had been made by the petitioner) on the ground that the Petitioner had filed some papers on the date of hearing which could not take place on account of pre-occupation of the authorities. The Court held that filing of papers cannot be equated with personal hearing, and on this count alone, the order of the adjudicating authority passed on de-novo consideration of the matter was liable to be quashed.[1986(25) ELT-II(ALL)].

In Banwarilal Roy's case [AIR (1948) Calcutta 776] the Calcutta High Court laid down that:

"a judicial or quasi-judicial act on the other hand implies more than mere application of the mind or the formation of the opinion. It is a reference to the mode or manner in which that opinion is formed. It implies a 'proposal', an 'opposition' and the 'decision' on the issue."

In *Soorajmal v. Assistant Collector of Customs* [AIR (1952) Calcutta 103] the Calcutta High Court laid down that:

"It is the duty of the customs authorities to 'adjudge' (i.e. decree judicially) the penalty. In other words, to act judicially or quasi-judicially. The fundamental rules of judicial procedure or the principles of natural justice require that a proper hearing and opportunity be given to the person before the rights of such a person are affected by any decision or adjudication. Where the customs authorities impose extra duty, acting in a high handed and an arbitrary manner, arrive at their decisions on extraneous and irrelevant considerations without giving proper opportunity to the petitioner to put his case before the customs authorities and later on demand the extra duty, there has been a denial of natural justice and violation of the fundamental principles of judicial procedure and a writ of certiorari does lie even though there may be an alternative remedy open to the petitioner by way of an appeal".

The Calcutta High Court while observing as above relied on the Supreme Court decision in *Province of Bombay v. Khushaldas Advani* [AIR (1950) S.C. 222] and came to the aforesaid conclusion.

Classification of goods is an intricate but well defined exercise. Reading and interpreting a tariff entry cannot be done in any casual or non challant manner.

Words and expressions found in a tariff have to be properly understood and harmonized. They cannot be taken out and read in vacuum, so to say, nor can entries be read, out of context.

In *Ex-QUIZ TI v. State of Tamil Nadu* [1986 (25) ELT 6 (MAD)] the Madras High Court observed: "...the Supreme Court held that in determining connotation of words and expressions describing an article or commodity.... which is taxed..... if there is one principle fairly well settled, it is that the words or expressions must be construed in the sense in which they are understood in that trade by the dealer and the consumer and that it is they who are concerned with it, and it is the sense in which they understand it that constitutes the definite index of the legislative intention when the statute was enacted".

In Madanvathi's case [AIR (1960) Mysore 299, 301] the Mysore High Court (as it then was) pointed out that:

"the first and foremost rule of interpretation is the rule of grammatical interpretation,, the legislature must be deemed to have intended what it has said. It is no part of the duty of the court to presume that the legislature meant something other than what it said. If the words of the section are plain and unambiguous then there is no question of interpretation or construction. The duty of the Court is to implement these provisions".

In *Indye Chemicals v. Collector of Central Excise Ahmedabad* -1986 (25) ELT 318 (Tribunal), it has been reiterated that Exemption notifications are to be construed strictly and in accordance with the plain meaning of the words used therein and if there is any doubt, the benefit of that doubt should go to the assessee so that the tax burden is reduced.

In Goolabchand's case [AIR (1951) MB 11 (FB)] it has been laid down that:

"If a plain word carried a plain sense in the English language, however strict the law may interpret it, it will not ignore the ordinary meaning which it carries".

Crawford an authority on statutory construction has stated that:

"Where a word used by the legislature has fixed technical meaning; it is to be taken in that sense. The technical words and phrases of the law are presumed to have been used in their proper technical signification when used in statutes....."

Maxwel in his interpretation of statutes has stated that:

"the first and foremost elementary principle is that it is to be assumed that the words and phrases of technical legislation are used in their technical meaning if they have acquired one otherwise in their ordinary meaning".

In *United States v. Brown* [333 US (8)], it has been laid down : "no rule of construction necessitates acceptance of an interpretation of a statute resulting in absurd consequences".

In *Robertson v. Day* (5AC 62, 69) the privy Council has said:

"It is a legitimate rule of construction to construe words.....with reference to the words found in immediate connection with them".

In *Commissioner of Income Tax, Bombay v. Reid* (AIR (1931) Bombay 333) it has been laid down that:

“In construing a taxing Act, the Court is not justified in straining the language in order to hold a subject liable to tax”.

The Supreme Court in *Sales Tax Commissioner v. Modi Sugar Mills* [AIR (1901) SC 4047] laid down that:

“In interpreting a taxing statute equitable considerations are entirely out of place. Nor can taxing statutes be interpreted on any presumptions or assumptions. The Court must look squarely at the words of the statute and interpret them. It must interpret a taxing statute in the light of what is clearly expressed, it cannot imply anything which is not expressed; it cannot import provisions in the statute so as to supply any assumed deficiencies.”

The CEGAT, in *Venus Engineering Pvt. Ltd. v. Collector of Central Excise, Baroda* [1986 (25) ELT 553 (TRIBUNAL)] observed that it is hazardous to interpret a word in accordance with its definition in another statute or statutory instrument, more so when these are not dealing with any cognate subject. The subject of the Factories Act is far from being cognate with the subject of the Central Excise Act - one deals with taxes and the other with places where goods are manufactured. In the circumstances, the word “worker” in the Central Excise Act must be given the same meaning which it receives in ordinary parlance or is understood in the sense in which people conversant with the subject matter understand it and not that attributable to it under the Factory Act.

In the matter of availment of exemptions, it has been laid down by the Kerala High Court in the case of *Rice and Oil Mills* [1981 ELT (KER) 59] that denial of an exemption notification would tantamount to violation of fundamental right. It is also a settled legal position that in the matter of exemption notifications, the authorities cannot abridge, alter, amend or nullify the scope of a valid notification. Benefits flowing out of a valid notification cannot also be denied. An importer who does not have sufficient finances to clear the goods or if he does not require all the goods imported for consumption at one time, may file a Bill of Entry for warehousing under the warehousing provisions, so that appropriate duty may be paid at the time of actual clearance of the goods from the warehouse.

(b) Customs Act and Exemption Notifications

It has already been seen that under the Customs Act (Section 25 of the Act) power has been conferred on the Central Government to exempt certain goods from the levy of customs duty. An importer has to necessarily keep a proper track of exemption notifications. The exemptions notifications may either be without any reference to any given time period or may be with reference to a particular period. In the former case, the exemption notification can be withdrawn at any time by Central Government. It is therefore necessary to envisage this eventually while negotiating contracts for sale of goods after their import into India, because Customs Duty liability will increase the cost of import which should normally be reflected in selling price. Even if the imported goods are not to be sold but are to be captively consumed, the levy of import duty by withdrawing the exemption granted earlier

would have the effect of increasing the cost of production. If the imported goods are Plant and Machinery even then its effect would be to increase the cost of project. Even in a case where exemption has been given for a given period of time, the Central Government may withdraw the exemption notification before the expiry of the given period of time. To take an example, an exemption notification issued on 1.10.96 effective up to 1.10.99, may be withdrawn by the Government before 1.10.99, with the result an importer who placed an order for import of goods in the hope that they are exempted from duty may be faced with the shocking problem to pay the duty because the exemption notification has been withdrawn before 1.10.99. Now the question is, whether such a withdrawal of exemption before the expiry of normal period up to which it must have run can be challenged on the ground of promissory estoppel. The Judicial view seems to be that promissory estoppel cannot be pleaded against the Government, because withdrawal of the exemption notification under Section 25 is in public interest and such a withdrawal is a legislative function. These aspects must be borne in mind whenever any goods are imported on the basis of an exemption notification.

(c) Customs Act and CENVAT

Yet another aspect of interest in customs law is that the countervailing duties payable on the import of certain goods have to be properly accounted for in the documents. Suitable endorsement of the intention to avail CENVAT credit must be made on the Bill of entry. This is because the same Bill of entry may not be used for claiming any duty drawback on exports. This is because CENVAT credit can be availed in respect of countervailing duties also. If the importer is a canalising Agency and the goods are supplied by the canalising Agency to the Manufacturer, such a manufacturer must impress upon the canalising agency for issue of a certificate in respect of countervailing duties paid on the goods. Only on the basis of such a certificate the manufacturer would be able to get CENVAT credit.

(d) Customs Act and Duty drawback

As regards exports are concerned a matter of subtle importance is the claims for duty drawback on the export of goods. The interesting question that has been agitated more than once before various judicial forums is, when does export takes place, whether on the export goods passing into the control of Customs Department or when the export goods reach the buyer located beyond the territorial waters of India. Judicial decision on this point are quite encouraging. The view is that once the export goods pass into the control of the Customs Department so as to be out of the control of the exporter any longer, the export is supposed to be complete. This issue is very important because there may be two eventualities.

After the export goods passes into the control of Customs Department and the goods have been boarded on the ship or have been kept for boarding on the ship, there may be a loss or destruction due to fire or action of the sea or due to any other cause. Secondly, though the goods are safely boarded on the ship, but before they cross the territorial waters of India, there may be loss or damage to the goods on board or the whole ship may be lost. In such situations, it is proper to cite judicial rulings wherein some of the High Courts declared that export is complete when the export goods pass to the customs control notwithstanding the fact that thereafter they get lost or destroyed before crossing the territorial waters of India.

(e) Customs Act and Record Keeping

Last but not the least is the proper documentation and record keeping. The maintenance of correct and proper records would avoid any penal action being taken by the excise department for non-compliance with any particular rule or notification. In this context, it is necessary to be conversant with various regulations rules and the forms prescribed under the customs laws. These have been adequately explained in the preceding study lessons. A tax planner would therefore labour to keep track of various amendments brought about to various rules forms etc. so that the records and registers are at all times in consonance with the statutory requirements.

8.3 EXCISE LAW AND TAX PLANNING

A proper tax planning exercise has to be done so as to ensure due compliance with the statutory provisions and also to reduce the incidence of duty to the minimum. In fact a proper tax planning exercise in Central Excise Law demands :

- (i) An in-depth knowledge of substantial provisions;
- (ii) A thorough knowledge of procedural formalities;
- (iii) A continuous follow-up of various Exemptions Notifications;
- (iv) Awareness to various Court Rulings; and
- (v) Ability to reason out and argue one's point of view.

At the outset it is a wiser part of discretion to avoid basing tax planning on very tenuous reasoning and controversial interpretations. At the same time when the rulings of the Courts carry considerable conviction it would not be advisable to ignore them. Wherever the planning is done on premises which may not find a favour with the Courts or the legislature ultimately, it is desirable to make suitable provisions in the accounts to meet the duty liability that may arise in future for past transactions. Alternatively, while entering into contract of sale of goods, a manufacturer may do well to provide in the contract note that, should additional demand of duty be made by the Government on him, the same would be recovered from the purchaser (this is however subject to the advisability of including such term from a purely commercially strategic point of view).

Some broad areas of tax planning with reference to Central Excise Laws are discussed herein below:

(a) Classification of goods

Indirect taxes are levied on goods either at ad valorem or at specific rate or a combination of the two. Irrespective of the type of duty, the rate and the amount of duty would in almost all cases inter alia depend on classification of the goods. As wrong classification of goods would lead to many complications, it is better to get the classification of goods decided by the department.

(b) Valuation

Valuation of excisable goods is a very important aspect of Central Excise Law. As many of the excisable goods attract ad valorem rates of duty, a manufacturer should be quite conversant with the relevant provisions in this regard under the

Central Excise Act and the Rules. As on 1.7.2000, the new Section 4 substituted by the Finance Act, 2000 read with Valuation Rules, 2000 framed thereunder apply to such cases. In nutshell, the new provisions seek to tax the goods based on "transaction value" and barring the substitution of the basis of value from "normal price" to "transaction value" and some alteration in the definition of the terms "related person" and "place of removal", the provisions of valuation under the new law substantially remain the same. Suffice here to say that the manufacturer should try to meticulously plan the pricing of its products, as the prescription under the new law is that, so long as the price is the sole consideration and the buyer is not related to the assessee, then on each removal the value should be the "transaction value". Meaning thereby as long as transaction is not tainted by either the relationship or any additional consideration whatever price is charged by the assessee is bound to be accepted by the Revenue. Since "transaction value", which is going to be the basis for determination of value in majority of the cases, refers to "price actually paid or payable", the whole lot of problems related to adjustment of the sale price for various abatements like discount, cost of packing, etc. required to be applied under the erstwhile law for arriving at the assessable value which gave rise to needless litigation at times, would become redundant.

Wherever transaction value is not applicable, i.e. as provided under clause (b) of Section 4(1) which says that in any other case, including case where the goods are not sold, the value is to be determined in terms of rules framed for this purpose, which are called "Central Excise Valuation (Determination of Price of Excisable Goods) Rules, 2000 where (i) time of delivery is different from the time of removal; or (ii) place of delivery is different from the place of removal; or (iii) buyer is a related person; or (iv) there is additional consideration flowing from the buyer to seller. The cases of removal which does not amount to sale could be stock transfers to depots or other units of the assessee, or captive consumption of excisable goods. Under these circumstances, the value has to be determined in terms of rules framed for the purpose.

A few aspects on abatements/additions under the new provisions as compared to the old provisions, to be kept in mind are:

1. Discount

Under the old Section 4(4)(d)(ii), all discounts allowed at the time of removal in accordance with normal trade practices were permitted to be deducted from the wholesale price. Under the substituted new law, the definition of transaction value refers to "price actually paid or payable", and thus, can be construed to mean that price actually paid is net of discount and hence, discount does not form a part of the price at all. The Board (Central Board of Excise and Customs) has, in its clarificatory circular, dated 30.6.2000 at para 9 states that "no reference to discount is necessary in new Section 4 as the duty is chargeable on the net price paid or payable". Thus, if in any transaction a discount is allowed on declared price of any goods and actually passed on to the buyer of the goods as per common practice, the question of including the amount of discount in the transaction value does not arise. Discount of any type of description given on any normal price payable for any transaction will therefore, not form part of the transaction value of goods, e.g. quantity discount for goods purchased, cash discount for prompt payment, etc."

2. Packing cost

Packing charges do not find a place in the scheme of the new valuation code, the distinction between disposable and durable/returnable packing, primary, packing, secondary packing, special secondary packing introduced by the Courts loses their relevance. Generally, under all statutes, which seek to tax commodities, packing cost has always been held includible in the assessable value. Para 12 of the Board circular, dated 30.6.2000 *ibid* states that all packing costs would be includible in the value.

3. Cost of after sale service, etc.

Special care may have to be taken under the new provisions in regard to certain 'post manufacturing expenses' with reference to inclusions or non-inclusions of such expenses earlier done based on the judgements in the cases of "Bombay Tyre International and MRF Ltd.". As per the definition of "transaction value" under the new law, use of the words "any amount" "in connection with..... any other matter" and "servicing" would bring within its scope many expenses which were hitherto considered excludible being post removal expenses. The definition not only includes actual payment but also any provision made for such expenses about which also one has to be very careful.

Excise concessions on export of excisable goods

Exporters of excisable goods are entitled to several benefits. Under the schemes available in the Excise Law, the exporter of excisable goods can avail following facilities:

- (a) To export excisable goods on payment of excise duty and to claim refund of such duties subsequent to the export.
- (b) To export the goods without paying excise duty but on the basis of a bond being executed to fulfill the obligation to export.
- (c) To claim rebate of duty paid on excisable goods used as inputs in the manufacture of goods which are exported.
- (d) To process excisable goods required as inputs for manufacture of goods to be exported, without paying duty on such inputs.

Besides, the CENVAT Scheme also contains in-built provisions to act as a major incentive for production for export, which the exporter can make use of.

Refund claims

The assessee should ensure that all refund claims are prepared in time so that the right to claim is not lost. Refund can be claimed within one year of the relevant date subject to the provisions of Section 11B of the Central Excise Act. Where an order of the Assistant Commissioner of Central Excise classifying the product under a particular tariff item, though appealable, is not challenged by the assessee, then the classification order is not liable to be questioned, and the matter is not to be reopened in a proceeding for refund, which is in the nature of execution of a decree/order. That is how the relevant question arising for answer in the appeal before the Supreme Court in *Collector of Central Excise, Kanpur v. Flock (India) Pvt. Ltd.* (Civil Appeal No. 2552 of 1989, decided on August 4, 2000) was answered by a

Division Bench of the Supreme Court comprising Mr. Justice B.N. Kirpal and Mr. Justice D.P. Mohapatra. So one has to be careful that excise classification by Assistant Commissioner becomes final if not appealed against and cannot be challenged in proceedings for refund.

8.4 CENVAT

CENVAT Scheme (which replaced erstwhile MODVAT Scheme) offers considerable scope of planning. A manufacturer intending to avail CENVAT may look for his requirements of various spares and components etc. in the small scale industry sector. This is because small scale units enjoy the benefit of exemptions from central excise duty/levy of duty at concessional rates. Where the items produced by the SSI unit happens to be duty exempt whereas the raw material is duty paid, and benefit of CENVAT credit of duty paid on the raw material can not be availed by the SSI unit. The manufacturer can procure the material himself and send the same to SSI unit for job work and avail the benefit of CENVAT credit of duty paid on the raw material. But in order to be able to avail these benefits it is essential for the manufacturer to ensure that the small scale unit from whom supplies are being obtained is one availing exemption from duty on the basis of the value of its clearances pursuant to a notification issued in this behalf.

It is equally essential for the manufacturer of final products to ensure that a small scale unit supplying parts and components pays duty at a concessional rate. In other words, where goods are obtained from small scale industrial units working under the applicable notification paying nil rate of duty (on its clearances up to exemption limit) the purchaser (finished goods manufacturer) would not be entitled to any credit under CENVAT. It therefore may become necessary for the finished goods manufacturer to impress on the small scale units not to avail any exemption from duty for clearances upto the exemption limit. The small scale unit would be only more willing not to avail duty exemption benefit if a purchaser makes a firm commitment to place the orders. The small scale unit can always opt for paying duty if its own eligible inputs are dutiable and attract higher rate of duty than that payable on its finished products.

While working under the CENVAT rules, a manufacturer should ensure meticulous adherence to rules in regard to sending of goods for doing any job work or while sending the raw materials for manufacture of intermediate products under various notifications or while dealing with wastes.

Supply of decisions, drawings and specifications to other Manufacturers and permission to use Trade Mark

Sometimes manufacturers of reputed goods enter into agreements with other manufacturers, may be in the Small Scale Sector by which they undertake to supply drawings, designs under the specifications to ensure quality. To take a practical example, a manufacturer of reputed brand of electrical fans may supply essential specifications, designs and drawings relating to the manufacture and the manufacturer would adhere to the specifications and produce the electrical fans. The supplier of the drawings and designs may examine the quality and then buy the goods (fans) from the small scale manufacturer. In such cases the question that has been agitated before the courts has been that the supplier of drawing designs is the manufacturer and not the small scale unit which actually manufactures the goods (fans). The attempt of the revenue at times has been to include in the selling price of

the small scale industrial unit of the goods manufactured by it, the value of the trade mark of the supplier of the designs and drawings. Trade mark may be either affixed by the small scale unit itself or by the supplier. Supplier of drawings and designs cannot be regarded as manufacturer because under the excise law only a person who is actually manufacturing the excisable goods can be regarded as manufacturer provided such a manufacturer is not a dummy. And once the manufacture has been done by the SSI unit and it sells the goods on a principal to principal basis, for a purely commercial consideration, to the supplier of drawings and designs, there cannot be any further addition to the value of the excisable goods, attributable to the Trade Mark of the supplier of drawings and designs. Reference may be made on these points to following case laws—*Union of India and Others v. Cibatual Ltd.* 1985 22 ELT 302 (SC); *Joint Secretary of Government of India v. Food Specialities Ltd.* 1985 22 ELT 324 (SC); *Collector of Central Excise v. Modo Plant (P) Ltd.* 1985 21 ELT 187 (CEGAT); *Jay Engg. Works Ltd. v. Collector of Central Excise* 1985 21 ELT 299 (CEGAT); *Lucas Indian Service Ltd. v. Collector of Central Excise* 1984 16 ELT 415 (CEGAT).

With the result the Small Scale Unit may either pay no duty (if covered under the relevant applicable notification) up to the exemption limit or may pay concessional rates of duty. In either event there is double benefit. One, a lower assessable value due to a lower selling price which in return is a result of lesser cost of production, and other, a lower duty incidence in view of special benefits extended to small scale units. The manufacturers in the large scale sectors may profitably exploit such methods of decentralising production. There is however a note of caution that such decentralised production centres should not be mere dummies.

Show-cause notices

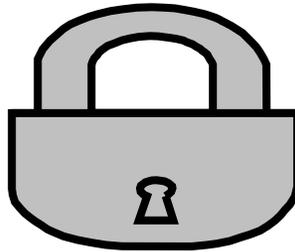
Show cause notices are quite common though may not be very frequent. A show cause notice pertaining to a demand of a higher duty emanates invariably under Section 11 A of the Central Excise Act, 1944. As per the section, for such recoveries a time limit has been prescribed. On receipt of the show cause notice an assessee first of all should ensure whether it has been issued by the proper authority having jurisdiction to issue show cause notice. For instance, the show cause notice which has to be issued by Commissioner Excise has been issued by the Assistant Commissioner of Central Excise. This show cause notice should be set aside for want of jurisdiction. This want of jurisdiction must be brought to the notice of authority, if need be the writ, jurisdiction of the High Courts can be invoked under Article 226 of the Constitution to set aside the show cause notice. Once the show cause notice is set aside a subsequent show cause notice issued by a proper authority cannot have a retrospective effect or have the effect of validating the show cause notice issued earlier by an authority without jurisdiction, even though the subject matter of the show cause notice may have many merits favouring the Revenue.

It would be better for the assessee to disclose all the relevant information to the excise department even while filing the classification list, other supporting documents/information so that at a later point of time the Excise Department does not allege fraud or mis-statement and invoke the five years period under Section 11A in demanding duties.

LESSON ROUND UP

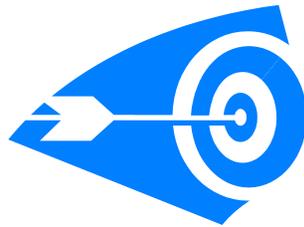
This Chapter includes :

- Promissory Estoppel in Fiscal Laws
- Customs Act and Tax Planning
- Excise Law and Tax Planning
- CENVAT

SELF-TEST QUESTIONS

1. What is the relevance of 'Doctrine of Promissory Estoppel' in the fiscal laws?
 2. What are the relevant areas in which tax planning could be done with regard to levy of duties of Customs?
 3. What is the scope of tax planning with regard to levies of the Central Excise?
 4. Explain briefly the provisions of CENVAT
-

STUDY IX
TAX PLANNING AND FINANCIAL MANAGEMENT DECISIONS



LEARNING OBJECTIVES

The objective of this Chapter is to discuss the following topics/concepts :

- Scope and Management in customs, with specific reference to important issues in the respective areas.
- Customs officials
- Exemption from Duty
- Refunds
- Authorities for Advance Ruling
- Clearance of Import & Export Duties
- Warehousing
- Customs Duty Drawback
- Baggage Rules

9.1 SCOPE AND MANAGEMENT IN CUSTOMS

Custom duty as we understand got its origin in the British period. As per historical records the Britishers established the first Board of Revenue in 1786 at Calcutta. A uniform tariff Act was introduced in 1859 all over India. Then Indian Tariff Act was passed in 1894 which was followed by Land Customs Act 1924. After independence custom law in our country has been consolidated comprising sea, water and air Acts into one Act. As stated earlier the Indian Tariff Act, 1934 was deficient in certain respects and as a result under the recommendation of the Tariff Revision Committee adopted Brussels trade Nomenclature of Customs Cooperative Council (CCCN) with modification to suit Indian conditions.

The Central Board of Excise and Customs (CBEC) is the authority controlling the operations relating to Customs Law in India. It consists of Commissionerates in different areas.

Customs duties include:

- (a) Basic Customs duty includes :
 - (i) Standard rate (this rate is charged where there is no provision for preferential treatment);
 - (ii) Preferential rate application to goods imported from any preferential areas as per agreement
- (b) Surcharge
- (c) Special Additional customs duty includes
 - (i) levied @ 4% under Section 3(5) of Customs Tariff Act, 1975
- (d) Additional duties also known as countervailing duty includes-
 - (i) levied under Section 3(1) & 3(3) of Customs Tariff Act, 1975.

9.2 SCOPE

The Customs Act 1962, was passed by Parliament on 13th December 1962. The Act came into force on February 1, 1963. The Act extends to the whole of India. It is a simple, crisp and lucid piece of enactment. It is primarily treated as a Revenue Act. Its main object is to collect duties on exports and taxes on imports under the fiscal laws and tariffs. The Customs Act consists of 17 Chapters and 161 Sections.

The Customs Act is aimed at preventing illegal imports and exports of goods which tend to cause distortions in the economy. It affords protection to home industries by means of regulating imports thereby conserving precious foreign exchange and promoting exports.

The Customs Act, 1962 contains provisions towards the following :

- (i) Enforcing various restrictions and prohibitions in respect of import and export of goods.*
- (ii) Levy, assessment and collection of import and export duties;*
- (iii) Quasi-judicial adjudication proceedings;*
- (iv) Appellate and Reversionary authority;*
- (v) Prosecution of offenders by the various courts.*

9.3 CUSTOMS OFFICIALS

The following are the classes of officers of customs, namely :

- (a) Chief Commissioners of Customs
- (b) Commissioners of Customs
- (c) Commissioners of Customs (Appeals)
- (d) Deputy Commissioners of Customs
- (e) Assistant Commissioners of Customs
- (f) Such other class of officers of Customs as may be appointed for the purposes of this Act.

An officer of customs may exercise the powers and discharge the duties conferred or imposed on him under this Act, subject to conditions of the CBE&C.

An officer of customs may exercise the powers and discharge the duties conferred or imposed under this Act on any other officer of customs who is subordinate to him.

A Commissioner (Appeals) shall not exercise the powers and discharges the duties conferred or imposed on an officer of Customs other than those specified in Chapter XV and Section 108.

The Central Government may, by notification in the Official Gazette, appoint—

- (a) the ports and airports which alone shall be customs ports or customs airports for the unloading of imported goods and the loading of export goods or any class of such goods.
- (b) the places which alone shall be inland container depots for the unloading of imported goods and the loading of export goods or any class of such goods.
- (c) the places which alone shall be land customs stations for the clearance of goods imported or to be exported by land or inland water or any class of such goods.
- (d) the routes by which alone goods or any class of goods specified in the notification may pass by land or inland waters into or out of India, or to or from any land customs station from or to any land frontier.
- (e) the ports which alone shall be coastal ports for the carrying on of trade in coastal goods or any class of such goods with all or any specified ports in India.

9.4 EXEMPTION FROM DUTY

Section 25(1) of the Customs Act, 1952 authorises Central Government to exempt partly or wholly any goods subject to duty of persons in public interest. This is done by issue of notification in the Official Gazette. Likewise Central Government has the power to grant adhoc assumptions under section 25(2) of the Act. It become effective from the state mentioned in the notification in the case *Jain Sudh Vanaspati v. Union of India* the Supreme Court has pointed out that the Central Government is empowered to modify or withdraw the exemption and while doing so it will not effect the principal of promissory estoppel. Section 25 has been amended from time to time.

Adhoc exemptions can be granted to the following items :

- (i) life saving drugs;*
- (ii) article imported for handicap persons;*
- (iii) imports by Indian Navy;*
- (iv) import of research material;*
- (v) import of trophies and cups etc.*

Passing of Finance Act, 1999 is specified capital goods/consumables imported by ONGC/OIL for petroleum operations have exempted at par imposed under NELP lease agreement.

9.5 REFUNDS

Section 27 of the Customs Act deals with the refund of the duty. As per this section—

- (1) Any person who has paid the duty or interest or who has borne the incidence of duty or interest can claim refund of duty by way of application.
- (2) The application for refund is to be made to the Assistant Commissioner of customs or Deputy Commissioner of customs.
- (3) The application should be made before the expiry of one year from the date of payment of such duty or interest. However the limitation period of one year shall not apply where duty or interest is paid under protest.
- (4) The application should be accompanied by such documentary or other evidence to establish that the amount of duty or interest in relation to which such refund is claimed was collected from, or paid by him and incidence of such amount is not transferred to any other person.

The period of one year shall be computed from the following date:

- | | | |
|---|---|--|
| (1) <i>In case goods are exempt from payment of duty by a special order under Sub-section (2) of Section 25</i> | — | <i>Date of issue of such order.</i> |
| (2) <i>Duty becomes refundable because of judgment, decree, order or direction of appellate authority, appellate tribunal, or court</i> | — | <i>Date of such judgment decree, order or direction</i> |
| (3) <i>Duty is paid provisionally under Section 18</i> | — | <i>Date of adjustment of duty after final assessment</i> |

9.6 AUTHORITIES FOR ADVANCE RULINGS

The Finance Act, 1999 has inserted a new chapter VB on authority for advance ruling in the customs act in order to provide a scheme for giving binding rulings in respect of activities of import and export involving non-residence in advance of the commencement of the activities so as to avoid needless litigation and promote better compliance with the conditions of the Act. As per section 28(H) an interested applicant desirous of obtaining an advance ruling can furnish his application under the provisions of the Act. Section 28(I) deals with procedural aspect on the receipt of application and Section 28(K) deals with certain circumstances where advance ruling is taken as void.

9.7 CLEARANCE OF IMPORT & EXPORT DUTIES

Section 46 of the Customs Act lays down the procedure of how importers of any goods other than goods which are to be transhipped shall make an entry in a Bill of Entry for home consumption or warehousing, A Bill of Entry under section 46(9) may

be presented at any time after the delivery of import manifest or import report as the case may be. The importer while presenting a Bill of Entry shall at the foot thereof make an subscribe to a declaration as to the truth of contents of the Bill of Entry and shall in support of such declaration reduced to the proper officer, the invoice if any, related to the imported goods.

There are three kinds of entries namely :

- (i) Bill of Entry for home consumption;*
- (ii) Warehousing Bill of Entry;*
- (iii) Bill of Entry for clearance ex-bonds.*

The procedure for clearance of goods stated in Section 30 of the Act. Sections 82, 83 and 84 of the Act deals with the clearance of the goods by post. There is provision in the Act relating to provisional assessment of the duty.

Regarding clearance of export goods GR Forms is used in duplicate to filed with the shipping bill. An applicant who is willing to export his goods is required to get from RBI "exporter code number". The number is required to quoted invariably on all the export forms. The RBI would outright reject the export forms not having the prescribed code number. The GR forms are supplied by the RBI through authorized banks. According to Section 40 of the Act the goods to be exported cannot be loaded unless it has been certified by a proper officer. There is provision for entry in the "entry outwards form". Section 29 states that export goods would not be loaded in a vessel until entry outward is granted. The exporter has to file shipping bill or bill of export to the proper authorities.

9.8 WAREHOUSING

The term "warehouse" under Section 2(43) of the Act to mean a public bonded warehouse appointed under Section 56 of the Customs Act or a private bonded warehouse licensed under Section 58 of the Customs Act. Public and private warehouses can be located at such warehousing stations as declared by CBEC. Sections 57 to 73 of Chapter IX deals with various positions pertaining to warehousing of imported goods. Section 59 of the Act requires an importer to execute a bond binding him in a sum equal to twice the amount of duty assessed on such goods:

- (i) observed all provisions of the Act and Rules;
- (ii) to pay charges with interest;
- (iii) to pay all penalties leviable for violations of provisions of the Customs Act.

The Finance Act, 2000 has amended Section 59 to has to increased the rate of interest payable in respect of imported goods to a maximum of 36% per annum. Section 63 of the Act deals with the payment of rent and warehouse charges.

Section 64 of the Act deals with the right of owner of the warehouse with prior approval of the proper officer deal with the goods stored in warehouse.

9.9 CUSTOMS DUTY DRAWBACK

The term drawback of duty is different from grant of refund of duty. "Drawback" in relation to any goods manufactured in India and exported means—

- (i) the rebate of duty chargeable on any imported materials or excisable materials used in the manufactured of goods in India or;
- (ii) the rebate of duty of excise chargeable under Central Excise Act, 1944 on the goods specified in schedule I;

Section 54 of the Act lays down that where an goods capable of being easily identified, have been imported into India and upon on which any duty has been paid according to the provisions of the Section 51, 77 and 82 of the Act.

The following has to be satisfied with regard claiming duty drawback. This includes :

- (i) The goods should be previously imported;*
- (ii) The goods can be identified;*
- (iii) The duty on import has been paid;*
- (iv) The goods has been properly cleared under authority of proper officer,*
- (v) The goods must be entered for re-export within two years from the date of duty. The Board may extend the period two years if sufficient cause has been shown to the authorities.*

9.10 BAGGAGE RULES

Chapter 11 of the Act contains provisions relating to baggage, goods imported/exported by post and stores. Under Finance Act, 2004 the rate of customs duty on dutiable baggage was 40% which was been reduced to 35% by the Finance Act, 2005. Baggage is exempt from CVD. However, education cess@2% and Secondary and higher education cess @1% is payable. Section 81 of the Act deals with regulation aspect with regard to baggage. The Government of India, Department of Revenue and Excise has framed:

- (i) Baggage Rules 1998;
- (ii) Tourist Baggage Rules 1978;
- (iii) Transfer of Residence Rules, 1978.

(1) Baggage includes unaccompanied baggage but does not include motor vehicles [section 2(3)].

Baggage includes all dutiable articles imported by passenger or crew but does not include motor vehicles, alcoholic drinks (beyond limits) and goods imported through courier.

(2) Duty free allowances generally allowed to the Indian resident or foreigner residing in India:

- For Indian resident or a foreigner residing in India and returning from countries other than Nepal, Bhutan, Myanmar or China through other than by specified land route:

Duty Free allowance for bonafide baggage consisting of	For passengers of age 10 years and above		For passengers of age below 10 years	
	Stay abroad for more than 3 days	Stay abroad for 3 days or less	Stay abroad for more than 3 days	Stay abroad for 3 days or less
Used personal effects (excluding jewellery) required for satisfying daily necessities of life	Free	Free	Free	Free
Articles other than those mentioned below at note no.(b) if carried on person or in the accompanied baggage	Free upto Rs. 25,000.	Free upto Rs. 12,000.	Free upto Rs. 6,000.	Free upto Rs. 3,000.

- For Indian resident or a foreigner residing in India and returning from countries from Nepal, Bhutan, Myanmar or China other than by specified land route or for Indian resident or a foreigner residing in India and returning from countries other than Nepal, Bhutan, Myanmar or China by specified land route:

Duty Free allowance for bonafide baggage consisting of	For passengers of age above 10 years and Stay abroad for more than 3 days	For passengers of age upto 10 years and Stay abroad for more than 3 days
Used personal effects (excluding jewellery) required for satisfying daily necessities of life	Free	Free
Articles other than those mentioned at note no.(b) if carried on person or in the accompanied baggage	Free upto Rs. 6,000.	Free upto Rs. 1,500.

Note:

- (a) The free allowance shall not be allowed to be pooled with the free allowance of any other passenger.

- (b) The free allowance is not applicable to the following goods:
- (a) Fire arms.
 - (b) Cartridges of fire arms exceeding 50.
 - (c) Cigarettes exceeding 200 or cigars exceeding 50 or tobacco exceeding 250 gms.
 - (d) Alcoholic liquor and wines in excess of 2 litre each.
 - (e) Gold or silver, in any form, other than ornaments.
- (c) The goods over and above the free allowances shall be chargeable to **customs duty @ 35% + an education cess of 3% i.e. to say the effective rate is 36.05%.**
- (d) In case the value of one item exceeds the duty free allowance, the duty shall be calculated only on the excess of such amount.

(3) Import of gold and silver as baggage

An Indian passenger who has been residing abroad for over one year is allowed to bring jewellery, free of duty in his bonafide baggage upto an aggregate value of Rs. 10,000/- (in the case of a gentleman passenger) or Rs.20,000/- (in the case of a lady passenger).

(4) Transfer of residence (TR)

A person who is transferring his residence to India shall be allowed clearance free of duty, in addition to allowances applicable to Indian residents or foreigners residing in India or to passengers returning from Nepal, Bhutan, Myanmar or China, other than by specified land route articles in bonafide baggage to the extent and subject to conditions as mentioned below :

Articles allowed Free of Duty	Conditions	Relaxation that may be considered
(a) Used personal and household articles other than those listed at Annex I* or Annex II**, but including (the articles listed at Annexure-III **) and Jewellery upto Rs. 10000 by a gentleman passenger or Rs. 20000 for a lady passenger	(1) Minimum stay of two years abroad, immediately preceding the date of his arrival on transfer of residence (2) Total stay in India on short visits during the 2 preceding years should not exceed 6 months, and (3) Passenger has not availed this concession in the preceding three years.	(a) For condition (1) Shortfall of upto 2 months in stay abroad can be condoned by Deputy / Assistant Commissioner of Customs if the early return is on account of - (i) terminal leave or vacation being availed of by the passenger, or (ii) any other special circumstances. (b) For condition (2) Commissioner of Customs

		may condone short visits in excess of 6 months in deserving cases. (c) For condition (3) No relaxation.
(b) Jewellery taken out earlier by the passenger or by a member of his family from India.	Satisfaction of the Assistant Commissioner of Customs regarding the jewellery having been taken out earlier from India.	-----

*** Annexure I**

1. Fire arms.
2. Cartridges of fire arms exceeding 50.
3. Cigarettes exceeding 200 or cigars exceeding 50 or tobacco exceeding 250 gms.
4. Alcoholic liquor or wines in excess of 2 litres.
5. Gold or silver, in any form, other than ornaments.

****Annexure II**

1. Colour Television or Monochrome Television.
2. Digital Video Disc Player.
3. Video Home Theatre System.
4. Dish Washer.
5. Music System.
6. Air Conditioner.
7. Domestic refrigerators of capacity above 300 litres or its equivalent.
8. Deep Freezer.
9. Microwave Oven.
10. Video camera or the combination of any such video camera with one or more of the following goods, namely:-
 - (a) Television Receiver;
 - (b) Sound recording or reproducing apparatus;
 - (c) Video reproducing apparatus.
11. Word Processing Machine.
12. Fax Machine.
13. Portable Photocopying Machine.
14. Vessel.
15. Aircraft.

16. Cinematographic films of 35 mm and above.
17. Gold or Silver, in any form, other than ornaments.

*****Annexure III**

1. VCR or VCP or VTR or VCDP.
2. Washing Machine
3. Electrical or LPG Cooking Range
4. Personal Computer (Desktop Computer)
5. Lap Top Computer (Notebook Computer)
6. Domestic Refrigerator upto 300 Ltr. Capacity or its equivalent.

(5) Baggage by foreign tourist coming to India and currency he can bring in

A tourist is a passenger

- (a) who is not normally a resident in India;
- (b) who enters India for a stay of not more than six months in the course of any twelve months period for legitimate non-immigrant purposes, such as :
touring, recreation, sports, health, family reasons, study, religious pilgrimage, or business;

A tourist arriving in India shall be allowed clearance free of duty articles in his bonafide baggage to the extent as mentioned below:-

Persons	Articles allowed free of duty
Tourists of Indian origin other than tourist of India coming by specified land route.	(i) Used personal effects and travel souvenirs, if- (a) These goods are for personal use of the tourist, and (b) These goods, other than those consumed during the stay in India, are re-exported when the tourist leaves India for a foreign destination. (ii) duty free allowances for articles as specified on Question no.
Tourists of foreign origin other than those of Nepalese origin coming from Nepal or of Bhutanese origin coming from Bhutan or of Pakistani origin coming from Pakistan.	(i) Used personal effects and travel souvenirs, if (a) These goods are for personal use of the tourist, and (b) These goods, other than those consumed during the stay in India, are re-exported when the tourist leaves India for a foreign destination. (ii) Articles upto a value of ₹ 8000/- for making gifts.

Tourists of Nepalese origin coming from Nepal or of Bhutanese origin coming from Bhutan.	No free allowance.
Tourists of Pakistani origin coming from Pakistan other than by land route or Pakistan origin of foreign tourists coming from by specified land route Indian origin coming by specified land route	(i) Used personal effects and travel souvenirs, if (a) These goods are for personal use of the tourist, and (b) These goods, other than those consumed during the stay in India, are re-exported when the tourist leaves India for a foreign destination. (ii) Articles upto a value of ₹6000 for making gifts.

(6) Unaccompanied baggage

The provisions of Baggage Rules are also extended to unaccompanied baggage except where they have been specifically excluded.

- (a) The unaccompanied baggage should be in the possession abroad of the passenger and shall be **dispatched within one month of his arrival in India** or within such further period as the Deputy / Assistant Commissioner of Customs may allow.
- (b) The unaccompanied baggage may land in India **upto two months before the arrival of the passenger or within such period, not exceeding one year** as the Deputy / Assistant Commissioner of Customs may allow, for reasons to be recorded, if he is satisfied that the passenger was prevented from arriving in India within the period of two months due to circumstances beyond his control, such as sudden illness of the passenger or a member of his family, or natural calamities or disturbed conditions or disruption of the transport or travel arrangements in the country or countries concerned on any other reasons, which necessitated a change in the travel schedule of the passenger.

LESSON ROUND UP

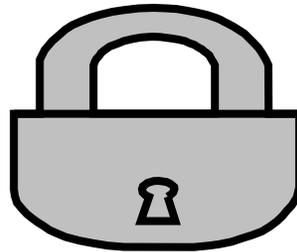


This Chapter includes:

- Scope and Management in customs, with specific reference to important issues in the respective areas.
- Customs officials

- Exemption from Duty
- Refunds
- Authorities for Advance Ruling
- Clearance of Import & Export Duties
- Warehousing
- Customs Duty Drawback
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SELF-TEST QUESTIONS

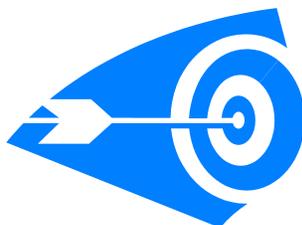


1. Explain briefly the scope of the Custom law in India .
2. What are the exemptions available under the customs Act 1962.
3. Discuss briefly the refund provisions under Customs Act 1962
4. Write short notes on the following :
 - (a) Warehousing procedures
 - (b) Duty Drawback provisions under customs law
 - (c) Baggage rules

PART C – INTERNATIONAL TAXATION

STUDY X

BASIC CONCEPTS OF INTERNATIONAL TAXATION



LEARNING OBJECTIVES

The objective of this Chapter is to discuss the following topics/concepts :

- An overview – from Indian perspective
- Tax havens;
- Double Taxation Relief;
 - (i) Bilateral and
 - (ii) Unilaterally
- Necessity for DTAA
- Transfer pricing,
- Controlled Foreign Corporation (CFC)
- The Sub Part F Regime;
- International mergers and acquisitions;

10.1 AN OVERVIEW – FROM INDIAN PERSPECTIVE

After the liberalization of Indian economy and easing of restrictions on the entry of foreign entities, cross border business transactions have increased manifold. With the ratification of WTO by the Government of India, our economy has become robust and an atmosphere has sprang up where FII investments in India have increased tremendously. All these economic activities has ramifications for tax laws of the country. Issues like tax havens, transfer pricing, double taxation, WTO, Subpart F, etc. are required to be taken care of and have become part and parcel of international taxation regime.

With the acceptance of the WTO regime India has embarked on the policy of market reforms and merging with the international business community by providing market access to the overseas investor with nil or qualitatively less restrictions.

In the context of international taxations, including cross border-investments, eliminated double taxation become an important consideration in doing business in India and abroad specially with the double taxation aspect became omnipresent in relations to transactions involving cross border investments with those foreign entities belonging to those countries with which India doesn't have double taxation avoidance agreements.

To overcome difficulties faced by investors from different countries, India in recent years entered into Double Taxation Avoidance Agreements (DTAA) with many countries. Our domestic statute namely, Income Tax Act, 1961 in the year 2001, introduced in the Income Tax Act, 1961 (Act hereinafter) elaborate legislation in Chapter X concerning transferring pricing to be discussed later issues. Section 91 of the Income Tax Act deals with unilateral relief given to the concerned persons of the countries with whom India does not have DTAA. DTAA under section 90 of the Act deals with general aspect concerning bilateral relief, multinational treaties and non-tax treaties.

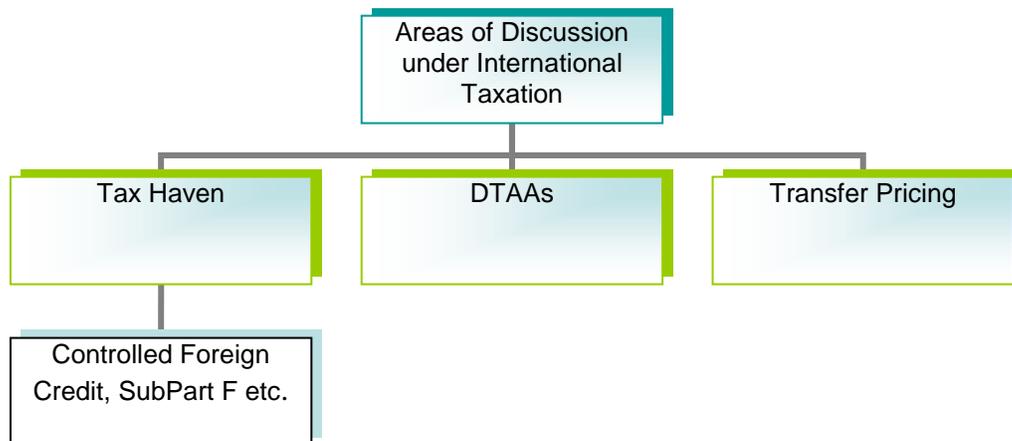
Another way of resolving disputes relating to taxes involving international transactions is through Mutual Agreement Procedure (MAP) in regard to those categories of disputes where there are no DTAA through OECD models and UN models regarding double tax avoidance agreements (the details of which are explained later). In order to reduce the misuse of tax havens, some countries have started the concept of CFC (controlled foreign corporations) to deal with the problems of tax evasion. There are nil tax haven destinations as well as low tax haven destinations.

The Income Tax Act, 1961 contains provisions to take care of transactions having extra-jurisdictional ramifications. Such as some incomes earned abroad by resident tax payers or income earned in India by NRI's and foreigners which generally are taxable in India under certain conditions. In the former case, incomes are taxed as per 'world wide income' principle, whereas in the latter case it is done through 'source principle'.

OECD-MC [Organization for Economic Co-operation and Development—Model Convention] defines double taxation as, "the imposition of comparable taxes in two (or more) states on the same tax payer in respect of the same subject matter and for identical periods".

In cases of double taxation the parties can get relief either through unilateral measures or bilateral measures or under adjudication by judiciary or through commercial arbitration.

Section 90 of the Income Tax Act, 1961 deals with agreements entered by Government of India with Government of other countries. Section 91 deals with provisions relating to those issues for which India does not have any formal agreements with Government of other countries, regarding avoidance of double taxation. Section 90A releases to granting of permissions to 'specified association'—through Official Gazette notification to enter into agreement with foreign Governments in regard to giving of relief for double taxation.



10.2 TAX HAVEN

A Tax Haven is a place where there is no tax on income or it is taxed at low rate. Individuals or corporate entities move from jurisdiction of high rates of taxes to the region of low tax in order to lower their overall tax liability. This has created competition amongst various governments of the world to lure more investments from abroad. Specially small countries are taking this opportunity to attract more investments from abroad. Many states have adopted different tax structures for different customers. It is like making 'tax haven shopping' available to large multinationals. This policy of the transnational corporates adversely affects the tax base of the country from where such entities transfer their business. It is a process adopted generally by large to medium sized multinationals to outmaneuver to pay lower taxes than those that would have been normally payable. Some critics call it as a method of tax avoidance. The modern concept of tax haven was started about 20 years ago by changing the focus from legislation to corporate vehicles which became pioneers in this field and are usually charged under local taxation (although they usually do not trade locally).

These vehicles are usually called 'exempt companies' or 'International Business corporations'. But in last ten years due to pressure from OECD, the tax haven countries have adjusted their domestic laws partially to check tax avoidance tax evasion practices.

10.2.1 Determining Factors of Tax Haven

The factors to be considered in taking decision whether a country is tax haven or not are:

1. *Nil or Nominal tax Rate*: There is no or nominal tax on income (generally or in specified circumstances).
2. *No Exchange of Information*: There is no system of exchange of information with respect to the tax regime in the tax haven country.
3. *Lack of Transparency*: The regime lacks transparency
4. *Limited Regulatory supervision*: No proper regulatory supervision and lack

of financial disclosures to the government would also categorise a country as Tax Haven.

5. The Government of the country facilitates the establishment of the foreign owned enterprises without the need for strict compliance of local laws or prohibits such entities from having any co mechanical impact on the local economy.

The OECD has outlined three parameters to consider whether a jurisdiction is tax haven or not.

- (a) *Rate of tax applicable*
- (b) *Withholding personal financial information.*
- (c) *Lack of transparency.*

Doing business through tax haven countries may not always be profitable. Some tax havens have become failure adventures or misadventures, like Beirut, Tangiers, Liberia, etc.

10.2.2 Methodology

The modus operandi followed in doing business through tax havens broadly, are as under :

- (a) **Personal Residency:** Where wealthy individuals reallocate themselves from high tax zones to low tax zones.
- (b) **Asset Holding :** It involves utilizing a trust or a company or a trust owing a company. Usually in this case, an entity from high tax jurisdiction transfers its assets to a trust in a low tax jurisdiction and settles his share in the trust on himself and later to his descendents without going through the vagaries of probate or inheritance tax.
- (c) **Business Activity:** Many corporate entities do not require locational or factor leverage to establish their business entities. Simply by transferring activities to low tax jurisdiction, they can earn 'margin' even though they are not performing any financial activity. They change their tax jurisdictions and through 'rein voicing' process they earn profit via investment in high tax jurisdictions. Example: Reinsurance companies.
- (d) **Financial Intermediaries :** Majority of business activities done in tax havens is through professional financial services such as mutual funds, banking, life insurance 'and pensions. Generally, the funds are deposited with the intermediary in the low tax jurisdiction and intermediary then on-lends or invests the money. Such systems do not normally avoid tax in the principle's customer jurisdiction; it enables financial service providers to provide multi-jurisdictional products without adding an additional layer of taxation. This has proved particularly useful in area of offshore funds.

Worldwide income of the Indian Resident's is taxable in India though section 91

of the Act provides relief by way of credit in respect of the tax paid on their foreign income if, the source is in the country with which there is no DTAA. Non-residents however are subject to source based taxation.

Some important destinations of tax havens are :

In USA – Delaware, Nevada, Wyoming, etc.

In Europe – Andorra, Canary, Lands, The Netherlands, Cyprus etc.

In Asia - Mauritius, Singapore, Dubai, etc.

In Africa : Capetown, Nairobi, etc.

10.2.3 Action taken to avoid harmful tax practices

OECD in May 1998 issued a report on Harmful Tax Competition and has made nineteen specific recommendations. Some of these are:

1. Adopt Controlled Foreign Corporation (CFC) or equivalent rules.
2. Consider Foreign information Reporting rules.
3. Enter into Tax Information Exchange Agreement (TIEA).
4. Apply the provisions of withholding tax when payments are made to offshore recipients.
5. Curbing treaty shopping term nation of existing treaties with tax havens like Mauritius.
6. Mutual assistance of tax authorities in the recovery of cross border tax claims etc.
7. More international co-operation by establishing forums to avoid harmful tax practice etc.

The following countries have committed to eliminate such practices, to embrace international standards of transparency to exchange in for duration to have fair competition:

(a) Bermuda; (b) The Cayman Islands; (c) Cyprus; (d) Malta; (e) Mauritius; (f) San Marino.

10.3 CONTROLLED FOREIGN CORPORATION (CFC)

The OECD recommended for adoption of CFCs Rules for taxing those entities which defer the tax liability after moving to the tax haven country. A CFC is a legal entity that exists in one jurisdiction but is owned or controlled primarily by taxpayers of a different jurisdiction. The CFC rules may also be termed 'anti-deferral rules'.

Income from a foreign source is taxed usually after it is accrued or received as income in the country of residence of the taxpayer. The use of intermediary entities in a tax-free or low-tax jurisdiction enables a tax resident to defer (or avoid) the domestic tax on the income until it is repatriated to the residence state.

This tax deferral could lead to an unjustifiable loss to the domestic tax revenue. As countries increasingly ease their exchange control rules, some have enacted Controlled Foreign Corporation rules to prevent the use of low-tax jurisdictions by their tax residents to defer the taxability of foreign income. Under the CFC rules, the domestic law effectively extends the residence rules to tax the income. It requires that the tax on profits, whether distributed or not, be paid by resident tax-payers. Normally, the CFC rules apply only to foreign companies controlled by residents, but certain countries extend it to foreign permanent establishments and trusts.

Many years ago, in the US, the incomes of foreign corporations were not taxed unless it was derived from US sources. In 1962, new tax laws were enacted to deter the use of foreign corporations as a way to avoid taxes. These rules have evolved into the complex rules referred to as the "controlled foreign corporation" rules.

CFCs are a legal consortium of the tax authorities around the world. If income is taxed at some point of time, then the taxpayer will have a greater after-tax retention of income if tax is paid during a future year as opposed to being paid in the present year. An anti-deferral tax regime could compel the foreign company to repatriate the profits, thus resulting in a favorable impact on the foreign exchange inflows as well as shoring up the domestic tax base.

The U.S, the UK, Germany and 25 other countries have adopted CFC regulations. Generally, the CFC regime is enacted by states in which tax liability is imposed on the worldwide income of resident taxpayers. Two operative factors are key to worldwide tax liability and to the generation of tax revenues on foreign source income, that is, the nexus between the state and the taxpayer; and the nexus between the taxpayer and the foreign income, the latter being more important vis-à-vis CFC.

Indian corporates not only scaled up the size of their overseas acquisitions but in several instances bought out companies much larger than them. The time now seems to be right to re-look the Controlled Foreign Corporation (CFC) recommendations of the Kelkar Working Committee Report on Tax Reforms in India.

10.4 SUB PART F

Sub Part F means special category of foreign source unearned income that is currently taxed by the Internal Revenue Code, 1986 of US whether or not it is remitted to the U.S. It is basically U.S. financial term used for the U.S. based institutions.

According to definition given under section 952 of the US Code by Legal Information Institute (Cornell University Law School), Sub Part F in "General" means in case of any foreign corporation, sum of :

- (1) insurance income (as defined under section 953),
- (2) the foreign base company income (as determined under section 954),
- (3) an amount equal to the product of—
 - (A) the income of such corporation other than income which—
 - (i) is attributable to earnings and profits of the foreign corporation

- included in the gross income of a United States person under section 951 (other than by reason of this paragraph), multiplied by
- (B) the international boycott factor (as determined under section 999),
 - (4) the sum of the amounts of any illegal bribes, kickbacks, or other payments (within the meaning of section 162 (c)) paid by or on behalf of the corporation during the taxable year of the corporation directly or indirectly to an official, employee, or agent in fact of a government, and
 - (5) the income of such corporation derived from any foreign country during any period during which section 901 (j) applies to such foreign country.

The payments referred to in paragraph (4) are payments which would be unlawful under the Foreign Corrupt Practices Act of 1977 if the payor were a United States person. For purposes of paragraph (5), the income described therein shall be reduced, under regulations prescribed by the Secretary, so as to take into account deductions (including taxes) properly allocable to such income.

Sub Part F was enacted in U.S., in 1962, through it has been amended many times but it retained its basic structure.

Sub Part F applies to certain income of "Controlled Foreign Corporations (CFC's)". CFC is a foreign corporation more than 50% of which by vote or value is owned by U.S. persons including U.S. citizens owning a 10% or greater interest in the corporation by VOTE (U.S. Shareholders). 'U.S. persons' includes U.S. citizens, residents, corporations, partnerships, trusts and estates. If a CFC has Sub Part F income, each U.S. shareholder must currently include prorates share of that income in its gross income as a deemed dividend.

Sub Part F rates attempt to prevent (or negate the tax advantage from) deflection of income, either from the United States or from the foreign country in which earned, into another jurisdiction which is a tax haven or which has a preferential tax regime for certain types of income. Thus, Sub Part F generally targets passive income and income that is split off from the activities that produced the value in the goods or services generating the income. Conversely Sub Part F does not require current taxation of active business income except when the income of a type that is easily reflected to tax haven, such as shipping income except when the income type earned in certain transaction of related parties. In related party transactions, deflections of is much easier because a unified group of corporations can direct the flow of income between entities in different jurisdictions.

A major category of Sub Part F income is Foreign Personal Holding Company Income (FPACI). This category includes interest, dividend, events and royalties. It also includes gains from the sale of property that produces passive income or that it is held for investment, gains from commodity transaction and gains from foreign company transactions as well as certain other income that is, in effect, the equivalent of interest or dividends. Because of its passive nature, such income often is highly mobile and can be easily deflected.

Income from the sale of the goods manufactured by the selling CFC is excluded from the FBSCI Rules. This exception is provided because, when the CFC performs the manufacturing generally, sales function has not been separated from

manufacturing function. However, because branches established in a separate jurisdiction can facilitate the deflection of income, the FBCSI provision contain a branch rule that treats income from the sale of goods manufactured by the CFC as FBCSI in certain cases when the selling and manufacturing, operation have been separated into different tax jurisdictions to obtain a lower rate of tax for the sale income.

Foreign base company services income is another category of Sub Part F income that applies to active income that can be deflected to a low tax jurisdictions through related party transactions, in this case, through the performance of Services FBCSI includes income from services performed outside the CFC's country of incorporation for or on behalf of related person. These rules are generally to address circulation in which service activities are separated from other business activities of a compensation into a separate subsidiary located in another jurisdiction to obtain a lower rate of tax for the services income.

This result can occur not only when the CFC perform the services for an unrelated person. Thus, the regulations contain 'a substantial assistance' rate under which if a related person provides the CFC with substantial assistance contributing to the performance of the services will be treated as performed for on behalf of a related person.

Source: The aforesaid is the extracts from, "The Deferral of Income Earned through U.S. Controlled Foreign Cooperatives. A policy study, upto pg xiv Office of Tax Policy Department of Treasury U.S. Government December 2000."

10.5 MEANING OF THE TERM 'RESIDENT OF CONTRACTING STATE'

Residence as defined in double taxation treaties is different from residence as defined for domestic tax purposes. Tax treaties generally follow the OECD Model Convention which provides:

For the purposes of this Convention, the term 'Resident of a Contracting State' means any person who, under the laws of that State, is liable to tax therein by reason of his domicile, residence, (UNMC also; place of incorporation), place of management or any other criterion of a similar nature, and also includes that State and any political sub-division or local authority thereof. This term, however, does not include any person who is liable to tax in that State in respect only of income from sources in that State or Capital situated therein.

Where by reason of the provisions of paragraph 1 an individual is a resident of both Contracting States, then his status shall be determined as follows:

- (a) he shall be deemed to be a resident only of the State in which he has a permanent home available to him; if he has a permanent home available to him in both States, he shall be deemed to be a resident only of the State with which his personal and economic relations are closer (centre of vital interests);
- (b) if the State in which he has his centre of vital interests cannot be determined, or if he has not a permanent home available to him in either State, he shall be deemed to be a resident only of the State in which he has an habitual abode;

- (c) if he has an habitual abode in both States or in neither of them, he shall be deemed to be a resident only of the State of which he is a national;
- (d) if he is a national of both States or of neither of them, the competent authorities of the Contracting States shall settle the question by mutual agreement.

Where by reason of the provisions of paragraph 1 a person other than an individual is a resident of both Contracting States, then it shall be deemed to be a resident only of the State in which its place of effective management is situated.

10.6 DOUBLE TAXATION RELIEF

The situation of double taxation will arise where the income gets taxed in two or more than two countries whether due to residency or source principle as the case may be. The problem of double taxation arises if the income of a person is taxed in one country on the basis of residence and on the basis of residency in another country or on the basis of both. To mitigate the double taxation of income the provisions of double taxation relief were made. The double taxation relief is available in two ways one is unilateral relief and other is bilateral relief.

Government of India can enter into agreement with a foreign government vide Entry 14 of the Union List regarding any matter provided Parliament verifies it. Double Tax Avoidance Agreement is a kind of bilateral treaty or agreement, between Government of India and any other foreign country or specified territory outside India. Such treaty or agreement is permissible in terms of Article 253 of the Constitution of India.

(a) Section 90: Agreements with Foreign Countries or specified territories

India has entered into bilateral agreements with many countries regarding avoidance of double taxation including tax avoidance and tax evasion issues. Section 90 of the income Tax deals with relief granted to assesses involved in paying taxes twice that is, paying taxes in India as well as in Foreign Countries or specified territory outside India.

As per section 90, the Central Government may enter into an agreement with the Government of any country outside India or specified territory outside India:

- (a) for granting relief in respect of
 - (i) income on which tax have been paid both under Income Tax Act,1962 and Income-Tax Act prevailed in that country or specified territory or
 - (ii) income-tax chargeable under Income Tax Act, 1962 and under the corresponding law in force in that country or specified territory to promote mutual economic relations, trade and investment, or
- (b) for the avoidance of double taxation of income under Income Tax Act, 1962 and under the corresponding law in force in that country or specified territory.
- (c) for exchange of information for the prevention of evasion or avoidance of income-tax chargeable under Income Tax Act, 1962 or under the corresponding law in force in that country or specified territory, or investigation of cases of such evasion or avoidance, or

- (d) for recovery of income-tax under Income Tax Act, 1962 and under the corresponding law in force in that country or specified territory

Where the Central Government has entered into an agreement with the Government of any country outside India or specified territory outside India for granting relief of tax, avoidance of double taxation, then, the provisions of Income Tax Act, 1962 shall apply to the assessee to whom such agreement applies, to the extent they are more beneficial to him.

All relief's announced by the Union Government are through Official Gazette. It has been stated in the provision that charge of tax in respect of a foreign company at a higher rate than the rate at which a domestic company is chargeable shall not be regarded as less favourable charge or levy of tax in respect of such foreign company.

(b) Section 90A

The Central Government is empowered by section 90A to enter into an agreement with any specified association in the specified territory outside India and the Central Government has been authorized to make such provisions as may be necessary for adopting and implementing such agreement. The provisions may be made:

- (a) for granting relief in respect of
- (i) income on which tax have been paid both under Income Tax Act, 1962 and Income-Tax Act prevailed in that specified territory or
 - (ii) income-tax chargeable under Income Tax Act, 1962 and under the corresponding law in force in that specified territory to promote mutual economic relations, trade and investment, or
- (b) for the avoidance of double taxation of income under Income Tax Act, 1962 and under the corresponding law in force in that specified territory.
- (c) for exchange of information for the prevention of evasion or avoidance of income-tax chargeable under Income Tax Act, 1962 or under the corresponding law in force in that specified territory, or investigation of cases of such evasion or avoidance, or
- (d) for recovery of income-tax under Income Tax Act, 1962 and under the corresponding law in force in that specified territory

Where the Central Government has entered into an agreement with the specified association of any specified territory outside India for granting relief of tax, avoidance of double taxation, then, the provisions of Income Tax Act, 1962 shall apply to the assessee to whom such agreement applies, to the extent they are more beneficial to him.

“Specified Association” for this section means any institution, association or body whether incorporated or not, functioning under any law for the time being in force India or the laws of specified territory outside India and which may be notified as such by the Central Government.

“Specified Territory” means any area outside India which may be notified as such by the Central Government for the purpose section 90A. The provision under this section will apply to the assesseees to the extent these are beneficial to them. This section provides relief in respect of double taxation in respect to countries with which India has no DTAA.

(c) Section 91

In any previous year, a person resident in India, has paid tax in any country with which India has no bilateral agreement under Section 90 for the relief or avoidance of double taxation in respect of his income which accrued or arose during that previous year under the law in force in that country, by deduction or otherwise, he shall be entitled to the deduction from the Indian Income Tax payable by him calculated on such doubly taxed income at this Indian Rate of Tax or the rate of the said country which ever is lower or at Indian rate of tax, if both rates are equal.

In case of the assessee stated above earns income from agricultural operation in Pakistan and paid tax thereof can seek relief at rate being lower of the following alternatives namely :

- (i) Tax actually paid in Pakistan
- (ii) Amount computed under Indian Tax Rates.

If any non-resident person is assessed on his share in the income of a registered firm assessed as resident person in India in any previous year and such share includes any income accruing or arising outside India during that previous year (and which is not deemed to accrue or arise in India) in a country with which there is no agreement under Section 90 for the relief or avoidance of double taxation and he proves that he has paid income tax by deduction or otherwise under the law in force in that country in respect of the income so included he shall be entitled:

- to a deduction from the Indian income tax payable by him of a sum calculated on such doubly taxed income so included
- at the Average Indian Income Tax Rate or
- the Average Foreign Tax Rate ,

Whichever is lower or at the Indian rate of tax if both the rates are equal.

Indian Tax on doubly taxed income:

$$\frac{\text{Tax on Total Income In India} \times \text{Doubly Taxed Income}}{\text{Total Income in India}}$$

Foreign Tax on doubly taxed income

$$\frac{\text{Tax Paid In Foreign Country} \times \text{Doubly Taxed Income}}{\text{Total Income in Foreign Country}}$$

Example:

Mr. Anuj an individual, resident of India in the previous year receives Professional fees of ₹ 1,70,000 on 7th August 2012 and ₹ 2,55,000 on 15th March 2013 for rendering services in Pakistan on which TDS of ₹ 30,000 and ₹ 45,000 have been deducted respectively. He incurred ₹ 1,60,000 as expenditure for earning this

fees. He paid ₹ 90,000 towards PPF. His Income from other sources is ₹ 2,60,000. Compute Tax liability & relief under section 91.

Solution:

**Computation of Relief under section 91 of Mr. Anuj
For the Assessment Year 2013-14**

1. Computation of tax liability of Mr. Anuj as per the Income Tax Act, 1962

	₹	₹
Income under the head business & profession:	5,00,000	
Less: Expenditure incurred	<u>1,60,000</u>	2,40,000
Income from other sources		<u>2,60,000</u>
Gross Total income		5,00,000
Less: Deduction u/s 80C: PPF		<u>90,000</u>
Total Income		<u>4,10,000</u>
Tax on ₹4,10,000		21,630
Less: Relief u/s 91		<u>12,661</u>
Tax Payable (rounded off)		<u>8,970</u>

2. Computation of relief u/s 91

Doubly Taxed Income = ₹ 2,40,000

Total Income in India = ₹ 4,10,000

Tax on total income in India = ₹21,630

Tax paid in foreign country = ₹75,000

Total income assessed in foreign country = ₹ 5,00,000

(a) Tax on such doubly taxed income in India:

$$\frac{21,630 \times 2,40,000}{4,10,000} = ₹12,661$$

(b) Tax on such doubly taxed income in foreign country:

$$\frac{75,000 \times 2,40,000}{5,00,000} = ₹36,000$$

Relief u/s 91 will be lower of (a) or (b) above i.e. ₹ 12,661/-

10.7 NECESSITY FOR DTAA

The need for Double Taxation Avoidance Agreement (DTAA) arises because of rules in two different countries regarding chargeability of income based on receipt and accrual, residential status etc. Double taxation is frequently avoided through DTAA's entered into by two countries for the avoidance of double taxation on the same income. The DTAA eliminates or mitigates the incidence of double taxation by sharing revenues arising out of international transactions by the two contracting states to the agreement. As there is no clear definition of income and taxability thereof, which is accepted internationally, an income may become liable to tax in two

countries. In such a case, the possibilities are as under:

1. The income is taxed only in one country.
2. The income is exempt in both countries.
3. The income is taxed in both countries, but credit for tax paid in one country is given against tax payable in the other country.

If the two countries do not have DTAA then in such a case, the domestic law of the country will apply. In the case of India, the provisions of Section 91 of the Income-Tax Act will apply. The Central Board of Direct Taxes has clarified vide Circular No.333 dated 2nd April, 1982 that in case of a conflict in the provisions of the agreement for Tax Avoidance of double taxation and the Income Tax Act, the provisions contained in the Agreement for Double Tax Avoidance will prevail.

“Economic Liberalization in India” as earlier started from 1991 has covered a wide area touching upon the different fields of international trade, exchange control, monetary and industrial policies, trade and fiscal policies, economic and cultural relations aimed at accelerating the growth in all spheres with a view to bringing about globalization of the India economy. The liberal and broad based economic and commercial relationship between India and various foreign countries in recent years had led to more collaboration and joint ventures at various levels in the public and private sectors to keep pace with the ever changing international advancement in trade, commerce, science and technology. The inflow of multinationals to setup business ventures in India coupled with the funds from Non-residents coming for short-term and long-term investments in India have helped to achieve a sound and stable economy and India today stands recognized internationally. The political situations due to changes in the Governments at the central and state levels have not adversely affected the growth of international trade and commerce between India and other countries.

The Government of India has entered into numerous tax treaties as well as trade agreements with various foreign countries to provide stability and certainty to the tax laws and commercial relationship between the parties in India and abroad. The large number of judicial pronouncements including advance rulings in the recent years under the tax laws, both direct and indirect, have added to the confidence of Non-residents being inspired with the Indian fiscal and judicial systems. The wealth of judicial decisions from the Supreme Court as well as the High Courts and the tribunals in deciding numerous tax disputes help to remove the uncertainties and ambiguities in the tax system and administration. The tax treaties have helped both the collaborators from abroad and the Indian enterprises in the private and public sectors to know precisely the nature, extent and scope of the tax liability as also the country in which tax is payable.

10.7.1 Taxation of Income from Air and Shipping Transport under DTAA

The DTAA is based on four basic models of DTAA and they are – OECD Model Tax Convention (emphasis is on residence principle), UN Model (combination of residence and source principle but the emphasis is on source principle), US Model (it's the Model to be followed for entering into DTAA's with the U.S. and its peculiar to the US) and the Andean Model (model adopted by member States namely Bolivia, Chile, Ecuador, Columbia, Peru and Venezuela).

Income derived from the operation of Air transport in international traffic by an enterprise of one contracting state will not be taxed in the other contracting state. In respect of an enterprise of one contracting state, income earned in the other contracting state from the operation of ships in international traffic, will be taxed in that contracting state wherein the place of effective management of enterprise is situated. However some DTA agreements contain provisions to tax the income in the other contracting state also, although at reduced rate.

These agreements follow a near uniform pattern in as much as India has guided itself by the UN model of double taxation avoidance agreements. The agreements allocate jurisdiction between the source and residence country. Wherever such jurisdiction is given to both the countries, the agreements prescribe maximum rate of taxation in the source country which is generally lower than the rate of tax under the domestic laws of that country. The double taxation in such cases are avoided by the residence country agreeing to give credit for tax paid in the source country thereby reducing tax payable in the residence country by the amount of tax paid in the source country. These agreements give the right of taxation in respect of the income of the nature of interest, dividend, royalty and fees for technical services to the country of residence. However the source country is also given the right but such taxation in the source country has to be limited to the rates prescribed in the agreement. The rate of taxation is on gross receipts without deduction of expenses.

10.7.2 The Concept of Permanent Establishment (PE)

One of the important terms that occur in all the Double Taxation Avoidance Agreements is the term 'Permanent Establishment' (PE) which has not been defined in the Income Tax Act. However as per the Double Taxation Avoidance Agreements, PE includes, a wide variety of arrangements i.e. a place of management, a branch, an office, a factory, a workshop or a warehouse, a mine, a quarry, an oilfield etc. Imposition of tax on a foreign enterprise is done only if it has a PE in the contracting state. Tax is computed by treating the PE as a distinct and independent enterprise.

Some Salient aspects concerning a PE could be discussed as under :

- PE is defined with reference to place and persons;
- PE could be a fixed place, a construction site, service PE, agency PE branch etc.
- PE denotes non-resident's business preserves. The degree of preserve which could constitute PE has been illustrated by 'inclusions and exclusions'.
- An enterprise is liable to tax on its profits in a foreign country, if it conducts its subsidiary in that country through PE.

Isolated or occasional transactions through some persons or agency do not create liability for tax is the basis of PE. There has to be continuity of activities contributing to the earning of income—something more than mere transaction of purchase and sale or transactions of preparatory or auxiliary nature. Such activities must be value creating activities requiring capital and lesson. 'Permanent' in PE does not mean everlasting.

In order to avoid double taxation it is provided that if a resident of India becomes liable to pay tax either directly or by deduction in the other country in respect of income from any source, he shall be allowed credit against the Indian tax payable in respect of such income in an amount not exceeding the tax borne by him in the other country on that portion of the income which is taxed in the said other country. The same benefit is available to the resident of the other Country, on income taxed in India.

10.8 TRANSFER PRICING

In the present age of globalization, diversification and expansion, most of the companies are working under the umbrella of group engaged in diversified fields/sectors leading to large number of transactions between related parties.

Related Party transaction means the transaction between/among the parties which are associated by reason of common control, common ownership or other common interest.

The mechanism for accounting, the pricing for these related transactions is called Transfer Pricing.

Transfer Price refers to the price of goods/services which is used in accounting for transfer of goods or services from one responsibility centre to another or from one company to another associated company. Transfer price affect the revenue of transferring division and the cost of receiving division. As a result, the profitability, return on investment and managerial performance evaluation of both divisions are also affected.

This may be understood well by the following example

1. Arihant & Companies is a group of Companies engaged in diversified business. One of its units i.e. Unit X is engaged in manufacturing of automotive batteries. Another Unit Y is engaged in manufacturing of Industrial Trucks. Unit X is supplying automotive batteries to Unit Y. In such cases transfer price mechanism is used to account for the transfer of automotive batteries.
2. XYZ Co. is expert in providing electrical and electronic services. It is engaged in providing support to its associated company as well as it is engaged in outsourcing contract. If XYZ Co. provides some services to its associated company, the transaction should be accounted at price calculated using transfer price mechanism.

Importance of Transfer Pricing

Transfer pricing mechanism is very important for following reasons:

1. Helpful in correct pricing of Product/Services - An effective transfer pricing mechanism helps an organization in correctly pricing its product and services. Since in any organization, transaction between associated parties occurs frequently, it is necessary to value all transaction correctly so that the final product/ services may be priced correctly.

2. **Helpful in Performance Evaluation :** For the performance evaluation of any entity, it is necessary that all economic transactions are accounted. Calculation of correct transfer price is necessary for accounting of inter related transaction between two Associated enterprises.
3. **Helpful in complying Statutory Legislations :** Since related party transaction have a direct bearing on the profitability or cost of a company, the effective transfer pricing mechanism is very necessary. For example, if the related party transactions are measured at less value, one unit may incur loss and other unit may earn undue profit. This will result in income tax imbalances at both parties end. Similarly, wrong transfer pricing may lead to wrong payment of excise duty, custom duty /sales tax (if applicable) as well.

Transfer Pricing Provisions in India

Increasing participation of multi-national groups in economic activities in India has given rise to new and complex issues emerging from transactions entered into between two or more enterprises belonging to the same group. Hence, there was a need to introduce a uniform and internationally accepted mechanism of determining reasonable, fair and equitable profits and taxes in India. Accordingly, the Finance Act, 2001 introduced law of transfer pricing in India through Sections 92 to 92F of the Income Tax Act, 1961 which guides computation of the transfer price and suggests detailed documentation procedures. Year 2012 brought a big change in transfer pricing regulations in India whereby government extended the applicability of transfer pricing regulations to specified domestic transactions which are enumerated in Section 92BA. This would help in curbing the practice of transferring profit from a taxable domestic zone to tax free domestic zone.

As stated earlier, the fundamental of transfer pricing provision is that transfer price should represent the arm's length price of goods transferred and services rendered from one unit to another unit.

What is Arm's Length Price?

In general arm's length price means fair price of goods transferred or services rendered. In other words, the transfer price should represent the price which could be charged from an independent party in uncontrolled conditions. Arm's length price calculation is very important for a company. In case the transfer price is not at arm's length, it may have following consequences

- A. Wrong performance evaluation
- B. Wrong pricing of final product (In case where the goods/services are used in the manufacturing of final product)
- C. Non compliances of applicable laws and thus attraction of penalty provisions.

The same may be explained with the following examples

Company X and Company Y is working under the common umbrella of Mohan & Company. Company X manufactures a product which is raw material for Company Y.

Case	Criteria	Effect on Company X	Effect on Company Y
1	Company X charges price more than the Arm's length price from Company Y	The revenue of company X will increase.	The total cost of company Y will increase. This will result into wrong pricing of its product which may further lead to uncompetitiveness of its product
2	Company X charges price less than the Arm's length price from Company Y	The revenue of company X will decrease. The parent company may close the company X treating it as loss making entity.	The total cost of company Y will decrease. Therefore, the company Y may charge lower price which may lead to loss at an entity level.
3	Company X charges Arm's Length price from Company Y	The revenue of company X will be representing true and fair view of its operation.	Company Y will be paying the price as equivalent to market price of Company X product and its cost will be correct. On the basis of the cost arrived after considering the arm's length price of company X product, company Y will be able to take correct price decision.

“The concept of associated enterprises and International transaction are very important for applying the transfer pricing provisions. Section 92A and Section 92B deals with these two important concepts of chapter X of Income Tax Act, 1961.”

Associated Enterprises (AE)

Associated Enterprises has been defined in Section 92A of the Act. It prescribes that “associated enterprise”, in relation to another enterprise, means an enterprise—

- (a) Which participates, directly or indirectly, or through one or more intermediaries, in the management or control or capital of the other enterprise; or
- (b) In respect of which one or more persons who participate, directly or indirectly, or through one or more intermediaries, in its management or control or capital, are the same persons who participate, directly or

indirectly, or through one or more intermediaries, in the management or control or capital of the other enterprise.

Thus, from above definition we may understand that

The basic criterion to determine an AE is the participation in management, control or capital (ownership) of one enterprise by another enterprise whereby the participation may be direct or indirect or through one or more intermediaries, control may be direct or indirect.

Deemed Associated Enterprises

As per Section 92(2), two enterprises shall be deemed to be associated enterprises if, at any time during the previous year,—

- (a) one enterprise holds, directly or indirectly, shares carrying not less than twenty-six per cent of the voting power in the other enterprise; or
- (b) any person or enterprise holds, directly or indirectly, shares carrying not less than twenty-six per cent of the voting power in each of such enterprises; or
- (c) a loan advanced by one enterprise to the other enterprise constitutes not less than fifty-one per cent of the book value of the total assets of the other enterprise; or
- (d) one enterprise guarantees not less than ten per cent of the total borrowings of the other enterprise; or
- (e) more than half of the board of directors or members of the governing board, or one or more executive directors or executive members of the governing board of one enterprise, are appointed by the other enterprise; or
- (f) more than half of the directors or members of the governing board, or one or more of the executive directors or members of the governing board, of each of the two enterprises are appointed by the same person or persons; or
- (g) the manufacture or processing of goods or articles or business carried out by one enterprise is wholly dependent on the use of know-how, patents, copyrights, trade-marks, licences, franchises or any other business or commercial rights of similar nature, or any data, documentation, drawing or specification relating to any patent, invention, model, design, secret formula or process, of which the other enterprise is the owner or in respect of which the other enterprise has exclusive rights; or
- (h) ninety per cent or more of the raw materials and consumables required for the manufacture or processing of goods or articles carried out by one enterprise, are supplied by the other enterprise, or by persons specified by the other enterprise, and the prices and other conditions relating to the supply are influenced by such other enterprise; or
- (i) the goods or articles manufactured or processed by one enterprise, are sold to the other enterprise or to persons specified by the other enterprise, and the prices and other conditions relating thereto are influenced by such other enterprise; or
- (j) where one enterprise is controlled by an individual, the other enterprise is

also controlled by such individual or his relative or jointly by such individual and relative of such individual; or

- (k) where one enterprise is controlled by a Hindu undivided family, the other enterprise is controlled by a member of such Hindu undivided family or by a relative of a member of such Hindu undivided family or jointly by such member and his relative; or
- (l) where one enterprise is a firm, association of persons or body of individuals, the other enterprise holds not less than ten per cent interest in such firm, association of persons or body of individuals; or
- (m) there exists between the two enterprises, any relationship of mutual interest, as may be prescribed

In Summary, two enterprises will be deemed as Associated Enterprises if

Quantum of Interest	Criteria applied for Associated Enterprises
26% or more	Shareholding with voting power – either direct or indirect
51% or more	Advancement of loan by one entity to other constituting certain percentage of the book value of the total assets of the other entity
51% or more	Based on the board of directors appointed by the governing board of the entity in the other
90% or more	Based on the quantum of supply of raw materials and consumables by one entity to the other
10% or more	Total Borrowing Guarantee by one enterprises for other
10% or more	Interest by a firm or association of Person(AOP) or by a body of Individual (BOI) in other firm AOP or firm or BOI

Meaning of International Transaction

International Transaction have been defined vide Section 92B of Income Tax Act. It provides that "International Transaction" means a transaction between two or more associated enterprises, either or both of whom are non-residents, in the nature of purchase, sale or lease of tangible or intangible property, or provision of services, or lending or borrowing money, or any other transaction having a bearing on the profits, income, losses or assets of such enterprises, and shall include a mutual agreement or arrangement between two or more associated enterprises for the allocation or apportionment of, or any contribution to, any cost or expense incurred or to be incurred in connection with a benefit, service or facility provided or to be provided to any one or more of such enterprises.

Deemed International Transaction

As per Section 92B(2) of Income Tax Act, A transaction entered into by an enterprise with a person other than an associated enterprise shall, for the purposes of sub-section (1), be deemed to be a transaction entered into between two associated enterprises, if there exists a prior agreement in relation to the relevant

transaction between such other person and the associated enterprise, or the terms of the relevant transaction are determined in substance between such other person and the associated enterprise.

Finance Act, 2012 has added an explanation for the purpose of Definition 92B and it provides that the expression "international transaction" shall include —

- (a) the purchase, sale, transfer, lease or use of tangible property including building, transportation vehicle, machinery, equipment, tools, plant, furniture, commodity or any other article, product or thing;
- (b) the purchase, sale, transfer, lease or use of intangible property, including the transfer of ownership or the provision of use of rights regarding land use, copyrights, patents, trademarks, licences, franchises, customer list, marketing channel, brand, commercial secret, know-how, industrial property right, exterior design or practical and new design or any other business or commercial rights of similar nature;
- (c) capital financing, including any type of long-term or short-term borrowing, lending or guarantee, purchase or sale of marketable securities or any type of advance, payments or deferred payment or receivable or any other debt arising during the course of business;
- (d) Provision of services, including provision of market research, market development, marketing management, administration, technical service, repairs, design, consultation, agency, scientific research, legal or accounting service;
- (e) A transaction of business restructuring or reorganization, entered into by an enterprise with an associated enterprise, irrespective of the fact that it has bearing on the profit, income, losses or assets of such enterprises at the time of the transaction or at any future date.

The term Intangible assets have also been elaborated and explanation to Section 92B provides that the expression Intangible shall include :

- (a) Marketing related intangible assets, such as, trademarks, trade names, brand names, logos;
- (b) Technology related intangible assets, such as, process patents, patent applications, technical documentation such as laboratory notebooks, technical know-how;
- (c) Artistic related intangible assets, such as, literary works and copyrights, musical compositions, copyrights, maps, engravings;
- (d) Data processing related intangible assets, such as, proprietary computer software, software copyrights, automated databases, and integrated circuit masks and masters;
- (e) Engineering related intangible assets, such as, industrial design, product patents, trade secrets, engineering drawing and schematics, blueprints, proprietary documentation;
- (f) Customer related intangible assets, such as, customer lists, customer contracts, customer relationship, open purchase orders;

- (g) Contract related intangible assets, such as, favourable supplier, contracts, licence agreements, franchise agreements, non-compete agreements;
- (h) Human capital related intangible assets, such as, trained and organized work force, employment agreements, and union contracts;
- (i) Location related intangible assets, such as, leasehold interest, mineral exploitation rights, easements, air rights, water rights;
- (j) Goodwill related intangible assets, such as, institutional goodwill, professional practice goodwill, personal goodwill of professional, celebrity goodwill, general business going concern value;
- (k) Methods, programmes, systems, procedures, campaigns, surveys, studies, forecasts, estimates, customer lists, or technical data;
- (l) Any other similar item that derives its value from its intellectual content rather than its physical attributes.'

The above explanation has added a wide range of Intangibles and the purpose of the explanation is to extend the applicability of Transfer pricing code to all International transaction involving the exchange of Intangibles which are not expressly available for trade .

Transfer Pricing – Applicability to Domestic Transactions

Honourable Supreme court in the case of *CIT v. Glaxo SmithKline Asia (P) Ltd.*, (2010) 195 Taxman 35 (SC) has advised that it needs to be considered whether the regulations should be applied to domestic transactions in cases where such transactions are not revenue-neutral. The facts and ruling of Honourable Supreme Court is following:

CIT v. Glaxo SmithKline Asia (P) Ltd., (2010) 195 Taxman 35 (SC)

Facts

1. Glaxo SmithKline Asia (P) Ltd (GSK) entered into an agreement with Glaxo Smith Kline Consumer Healthcare Ltd (“GSKCH”) whereby GSKCH would provide all administrative services relating to marketing, finance, Human Resource (HR) to GSK for cost +5% markup.
2. The AO disallowed a part of the charges reimbursed on the ground that they were excessive and not for business purposes. On appeal by GSK, CIT (Appeals) upheld the decision of AO.
3. GSK appeal to Income Tax Appellate Tribunal (ITAT) and ITAT ruled that AO has no power to disallow any expenditure as excessive or unreasonable unless the case falls within the scope of Section 40A(2). The revenue appeal to high court and revenue appeal was dismissed by High court.
4. For subsequent years AO continued to follow the same approach and GSK continued to get relief from ITAT. Having regard to the delay on the part of revenue to give effect to ITAT order GSK filled a writ petition before the High Court and High court issued direction to the Revenue to issue refund of taxes along with applicable interest.

Supreme Court Ruling

1. The revenue filed a Special Leave Petition (SLP) before the Honorable supreme court and supreme court held that since the exercise is revenue neutral and both the parties are not related parties in terms of Section 40A(2) of Income tax act, no interference is called for and the SLP filled by the Revenue is dismissed.
2. The honourable Supreme then stated that the larger issue is whether Transfer Pricing provisions should be limited to cross-border transactions or whether the Transfer Pricing Regulations be extended to domestic transactions. In domestic transactions, the under-invoicing of sales and over-invoicing of expenses ordinarily will be revenue neutral in nature, except in two circumstances having tax arbitrage such as where one of the related entities is (i) loss making or (ii) liable to pay tax at a lower rate and the profits are shifted to such entity;
3. The Supreme court further held that the complications arise in cases where the fair market value is required to be assigned to transactions between related parties u/s 40A(2). The Central Board of Direct taxes (CBDT) should examine whether Transfer Pricing provisions can be applied to domestic transactions between related parties u/s 40A(2) by making amendments to the Act. The AO can be empowered to make adjustments to the income declared by the assessee having regard to the fair market value of the transactions between the related parties and can apply any of the generally accepted methods of determination of arm's length price, including the methods provided under Transfer Pricing provisions. The law can also be amended to make it compulsory for the taxpayer to maintain Books of Accounts and other documents on the lines prescribed in Rule 10D and obtain an audit report from his Chartered Accountant (CA) that proper documents are maintained;
4. Finally it was held that though the Court normally does not make recommendations or suggestions, in order to reduce litigation occurring in complicated matters, the question of extending Transfer Pricing regulations to domestic transactions require expeditious consideration by the Ministry of Finance and the CBDT may also consider issuing appropriate instructions in that regard.

Specified Domestic Transactions

Finance Act, 2012 has made a very important change and it has extended the applicability of Transfer Pricing Provisions to specified domestic transaction w.e.f. 1st April, 2012.

The specified domestic party transactions would essentially include payment made by a company to a related person referred to in Section 40A(2)(b) of the Act including payment to a director of the company or any person who has a substantial interest in the company (that is, has a beneficial ownership of shares carrying not less than 20 per cent of voting power); transactions referred to in Section 80A(6) of the Act (for example, transfer of goods or services from a tax-incentivised unit/entity to a non-tax-incentivised unit/entity and vice-versa); and transactions referred to in

Section 80IA(8), 80IA(10) and 10AA(9) of the Act (carried out by industrial undertakings, infrastructure companies and units operating in special economic zones).

Section 92BA has been added in Transfer Price Code by Finance Act, 2012 which provides that

“Specified domestic transaction” in case of an assessee means any of the following transactions, not being an international transaction, namely:—

- (i) Any expenditure in respect of which payment has been made or is to be made to a person referred to in clause (b) of sub-section (2) of section 40A;*
- (ii) Any transaction referred to in section 80A;*
- (iii) Any transfer of goods or services referred to in sub-section (8) of section 80-IA;*
- (iv) Any business transacted between the assessee and other person as referred to in sub-section (10) of section 80-IA;*
- (v) Any transaction, referred to in any other section under Chapter VI-A or section 10AA, to which provisions of sub-section (8) or sub-section (10) of section 80-IA are applicable; or*
- (vi) Any other transaction as may be prescribed,*

and where the aggregate of such transactions entered into by the assessee in the previous year exceeds a sum of five crore rupees.’

Thus a specified domestic transaction means a transaction which is covered by criteria as given in section 92BA and the aggregate value of such transactions exceeds ₹5 crore in a year.

Transfer Pricing – Methods

Section 92C of Income Tax Act defines the methods which are to be used in determination of Arm's Length prices for International Transaction and specified domestic transaction. The arm's length price in relation to an international transaction/specified domestic transaction shall be determined by any of the following methods, being the most appropriate method, having regard to the nature of transaction or class of transaction or class of associated persons or functions performed by such persons or such other relevant factors as the Board may prescribe, namely :-

- (A) Comparable Uncontrolled Price Method (CUP)
- (B) Resale Price Method (RPM)
- (C) Cost Plus Method (CPM)
- (D) Profit Split Method (PSM)
- (E) Transactional Net Margin Method (TNMM)
- (F) Such other method as may be prescribed by the Board.

Various transfer pricing methods which are prescribed by Income Tax Act, 1961 are as under:

(A) Comparable Uncontrolled Price Method

Comparable Uncontrolled Price (“CUP”) method compares the price charged for property or services transferred in a controlled transaction to the price charged for property or services transferred in a comparable uncontrolled transaction in comparable circumstances.

An Uncontrolled price is the price agreed between the unrelated parties for the transfer of goods or services. If this uncontrolled price is comparable with the price charged for transfer of goods or services between the Associated Enterprises, then that price is Comparable Uncontrolled Price (CUP). This is the most direct method for the determination of the Arms’ length price.

Methods of CUP

CUP can be either

- (a) Internal CUP or
- (b) External CUP

Internal CUP is available, when the tax payer enters into a similar transaction with unrelated parties, as is done with a related party as well. This is considered a very good comparable, as the functions performed, processes involved, risks undertaken and assets employed are all easily comparable – more so, on “an apple to apple basis”.

The external CUP is available if a transaction between two independent enterprises takes place under comparable conditions involving comparable goods or services. For example an independent enterprise buys or sells a similar product, in similar quantities under similar term from / to another independent enterprise in a similar market will be termed as external CUP.

Applicability of the CUP Method

Comparable Uncontrolled Price method is treated as most reliable method of transfer pricing calculation but it is not easy to find the controllable price method easily. The CUP is believed to be the most reliable / best method, if one could identify and map it. CUP method can be applied without any difficulty in following circumstances.

- (1) Interest payment on a loan
- (2) Royalty payment
- (3) Software development where products are often licensed to a third party
- (4) Price charged for homogeneous items like traded goods

(B) Resale Price Method

Rule 10B (1) (b) of Income Tax Rules, 1962 prescribes Resale Price method by which,

- A. The price at which property purchased or services obtained by the enterprise from an associated enterprise is resold or are provided to an unrelated enterprise is identified;
- B. Such resale price is reduced by the amount of a normal gross profit margin accruing to the enterprise or to an unrelated enterprise from the purchase and resale of the same or similar property or from obtaining and providing the same or similar services, in a comparable uncontrolled transaction, or a number of such transactions;
- C. The price so arrived at is further reduced by the expenses incurred by the enterprise in connection with the purchase of property or obtaining of services;
- D. The price so arrived at is adjusted to take into account the functional and other differences, including differences in accounting practices, if any, between the international transaction and the comparable uncontrolled transactions, or between the enterprises entering into such transactions, which could materially affect the amount of gross profit margin in the open market;
- E. The adjusted price arrived at under sub-clause (iv) is taken to be an arms length price in respect of the purchase of the property or obtaining of the services by the enterprise from the associated enterprise.

Example

1. A sold a machine to B (Associated enterprise) and in turn B sold the same machinery to C (an independent party) at sale margin of 30% for ₹2,10,000 but without making any additional expenses and change. Here Arm's length price would be calculated as

Sales price to B	=	2, 10,000
Gross Margin	=	10,000 × 30% = 63,000
Transfer price	=	1, 47,000

2. A sold a machine to B (Associated enterprise) and in turn B sold the same machinery to C (an independent party) at sale margin of 30% for ₹4,00,000 but B has incurred 4000 in sending the machine to C. Here Arm's length price would be calculated as

Sales price to B	=	4, 00,000
Gross Margin	=	4,00,000 × 30%=1, 20,000
Balance	=	2, 80,000
Less: Expenses incurred by B	=	4,000
Arm's length price	=	2,76,000

(C) Cost Plus Method

Rule 10B (1) (c) of Income tax Rules, 1962 prescribes Cost Plus Method, by which,

- (i) The direct and indirect costs of production incurred by the enterprise in

respect of property transferred or services provided to an associated enterprise, are determined;

- (ii) The amount of a normal gross profit mark-up to such costs (computed according to the same accounting norms) arising from the transfer or provision of the same or similar property or services by the enterprise, or by an unrelated enterprise, in a comparable uncontrolled transaction, or a number of such transactions, is determined;
- (iii) The normal gross profit mark-up so determined is adjusted to take into account the functional and other differences, if any, between the international transaction and the comparable uncontrolled transactions, or between the enterprises entering into such transactions, which could materially affect such profit mark-up in the open market;
- (iv) The costs referred to in sub-clause (i) are increased by the adjusted profit mark-up arrived at under sub-clause (iii);
- (v) The sum so arrived at is taken to be an arm's length price in relation to the supply of the property or provision of services by the enterprise.

Under the Cost Plus Method, an arm's-length price equals the controlled party's cost of producing the tangible property plus an appropriate gross profit mark-up, defined as the ratio of gross profit to cost of goods sold (excluding operating expenses) for a comparable uncontrolled transaction.

The formulas for the transfer price in inter company transactions of products are as follows:

$$TP = COGS \times (1 + \text{mark-up}), \text{ where:}$$

- TP = Transfer Price of a product sold between a manufacturing company and a related company;
- COGS = Cost of goods sold of the manufacturing company
- Cost plus mark-up = gross profit mark-up defined as the ratio of gross profit to cost of goods sold

Gross profit is defined as sales minus cost of goods sold.

As an example, let us assume that the COGS in a transaction between two associated enterprises is ₹ 5,000. Assume that an arm's length gross profit mark-up that Associated Enterprise 1 should earn is 50%. The resulting transfer price between Associated Enterprise 1 and Associated Enterprise 2 is ₹7,500 [i.e. ₹ 5,000 × (1 + 0.50)].

In this method, calculation of cost of goods sold and gross margin are the most important factor.

(D) Profit Split Method

Rule 10B (1) (d) of Income tax Rules, 1962 prescribes Profit Split Method, which may be applicable mainly in international transactions involving transfer of unique intangibles or in multiple international transactions which are so interrelated that they

cannot be evaluated separately for the purpose of determining the arm's length price of any one transaction, by which:

- (i) The combined net profit of the associated enterprises arising from the international transaction in which they are engaged, is determined;
- (ii) The relative contribution made by each of the associated enterprises to the earning of such combined net profit, is then evaluated on the basis of the functions performed, assets employed or to be employed and risks assumed by each enterprise and on the basis of reliable external market data which indicates how such contribution would be evaluated by unrelated enterprises performing comparable functions in similar circumstances;
- (iii) The combined net profit is then split amongst the enterprises in proportion to their relative contributions, as computed above;
- (iv) The profit thus apportioned to the assessee is taken into account to arrive at an arm's length price in relation to the international transaction.

However, the combined net profit as determined in sub-clause (i) may, in the first instance, be partially allocated to each enterprise so as to provide it with a basic return appropriate for the type of international transaction in which it is engaged, with reference to market returns achieved for similar types of transactions by independent enterprises, and thereafter, the residual net profit remaining after such allocation may be split amongst the enterprises in proportion to their relative contribution in the manner specified under sub-clauses (ii) and (iii), and in such a case the aggregate of the net profit allocated to the enterprise in the first instance together with the residual net profit apportioned to that enterprise on the basis of its relative contribution shall be taken to be the net profit arising to that enterprise from the international transaction.

Two step Approach of Profit Split Method

Step 1: Allocation of sufficient profit to each enterprise to provide a basic compensation for routine contributions. This basic compensation does not include a return for possible valuable intangible assets owned by the associated enterprises. The basic compensation is determined based on the returns earned by comparable independent enterprises for comparable transactions or, more frequently, functions.

Step 2: Allocation of residual profit (i.e. profit remaining after step 1) between the associated enterprises based on the facts and circumstances. If the residual profit is attributable to intangible property, then the allocation of this profit should be based on the relative value of each enterprise's contributions of intangible property.

Example on the Profit Split Method (Residual Analysis Approach)

Company A is an Indian Company and deals in telecommunication products. It has developed a Microprocessor and it holds the patent for manufacturing of the microprocessor. Company B which is an overseas subsidiary of Company A is engaged in manufacturing of Mobile equipment at Australia. Company A supply the microprocessor to company B for using it in Mobile equipment and company B in turn after manufacturing the mobile sends the mobile to company "A" in India. Company A sells all the mobile in India.

Both companies contribute to the success of the mobile equipment through their design of the microprocessor and the equipment. As the nature of the products is

very advanced and unique, the group is unable to locate any comparable with similar intangible assets. Therefore, neither the traditional methods i.e. CUP Method, RSP Method nor the TNMM is appropriate in this case.

Nevertheless, the group is able to obtain reliable data on hand phone contract manufacturers and equipment wholesalers without unique intangible property in the telecommunication industry. The manufacturers earn a mark-up of 10% while the wholesalers derive a 25% margin on sales.

Company A's and Company B's respective share of profit is determined in 2 steps using the profit split method (residual analysis approach).

Step 1 – Determining the basic return

The simplified accounts of Company A and Company B are shown below:

	<i>Company B</i> (₹ in Lakhs)	<i>Company A</i> (₹ in Lakhs)
Sales	100	125
Cost of Goods Sold	(60)	(100)
Gross Margin	40	25
Sales, General & Administration Expenses	(5)	(15)
Operating Margin	35	10

The total operating profit for the group is ₹ 45 Lakhs.

Company B

<i>Particulars</i>	<i>Amount (₹ in Lakhs)</i>
Cost of goods sold	60
Margin @10%	6
Transfer price based on Comparable (without considering Intangibles)	66

Company A

<i>Particulars</i>	<i>Amount (₹ in Lakhs)</i>
Sales to third party customers	125
Resale margin of wholesalers comparables (without intangibles) @25%	31.25
Gross Margin	31.25

	<i>Company B</i> (₹ in Lakhs)	<i>Company A</i> (₹ in Lakhs)
Sales	66	
Cost of Goods Sold	(60)	
Gross Margin	6	31.25

Sales, General & Admin Expenses	(5)	(15)
Routine operating margin	1	16.25

The total operating margin of the group is ₹ 17.25 Lakhs.

Step 2 : Dividing the residual profit

The residual profit of the group is = ₹ 45 Lakhs – ₹ 17.25 Lakhs = ₹ 27.75 Lakhs

On further study of the two companies, two particular expense items, R&D expenses and marketing expenses, are identified as the key intangibles critical to the success of the mobile equipment. The R&D expenses and marketing expenses incurred by each company are:

Company A	12 Lakhs (80%)
Company B	3 Lakhs (20%)

Assuming that the R&D and marketing expenses are equally significant in contributing to the residual profits, based on the proportionate expenses incurred:

Company A's share of residual profit (80% × 27.75)
= ₹ 22.20 Lakhs

Company B's share of residual profit (20% × 27.75)
= ₹ 5.55 Lakhs

Therefore, the adjusted operating profit of

Company A is	=	₹ 22.20 L + ₹ 16.25 L = ₹ 38.45 Lakhs
Company B is	=	₹ 5.55 + ₹ 1 = ₹ 6.55 Lakhs.

The adjusted tax accounts are as follows:

	<i>Company B</i> (₹ in Lakhs)	<i>Company A</i> (₹ in Lakhs)
Sales	71.55	125
Cost of Goods Sold	(60)	(71.55)
Gross Margin	11.55	53.45
Sales, General & Admin Expenses	(5)	(15)
Operating Margin	6.55	38.45

Hence, the transfer price determined using the profit split method (residual analysis approach) should be ₹ 71.55 Lakhs

(E) Transactional Net Margin Method (TNMM)

Rule 10B (1) (e) of Income Tax Rules, 1962 prescribes, Transactional net margin method, by which,

- (i) The net profit margin realized by the enterprise from an international

transaction entered into with an associated enterprise is computed in relation to costs incurred or sales effected or assets employed or to be employed by the enterprise or having regard to any other relevant base;

- (ii) The net profit margin realized by the enterprise or by an unrelated enterprise from a comparable uncontrolled transaction or a number of such transactions is computed having regard to the same base;
- (iii) The net profit margin referred to in (ii) arising in comparable uncontrolled transactions is adjusted to take into account the differences, if any, between the international transaction and the comparable uncontrolled transactions, or between the enterprises entering into such transactions, which could materially affect the amount of net profit margin in the open market;
- (iv) the net profit margin realized by the enterprise and referred to in (i) is established to be the same as the net profit margin referred to in (iii);
- (v) The net profit margin thus established is then taken into account to arrive at an arms length price in relation to the international transaction.

Example

Nikhil & Co is an India manufacturer of dishwashers. All Nikhil & Co's dishwashers are sold to an overseas associated enterprise, Company G, and bears Company G's brand. Company G, a household electrical appliances brand name, sells only dishwashers manufactured by Nikhil & Co.

The CUP method is not applied in this case because no reliable adjustments can be made to account for differences with similar products in the market. After the appropriate functional analysis, Nikhil & Co was able to identify an Indian manufacturer of home electrical appliances, Company H, as a suitable comparable company. However, Company H performs warranty functions for its independent wholesalers, whereas Nikhil & Co does not. Company H realizes a net mark up (i.e. operating margin) of 10%.

As the costs pertaining to the warranty functions cannot be separately identified in Company H's accounts and no reliable adjustments can be made to account for the difference in the functions, it may be more reliable to examine the net margins in this case. The transfer price for Nikhil & Co's sale of dishwashers to Company G is computed using the TNMM as follows:

Nikhil & Co's cost of goods sold	₹ 5,000
Nikhil & Co's operating expenses	₹ <u>1,500</u>
Total costs	₹ 6,500
Add : Net mark up @ 10% (10% x 6,500)	₹ <u>650</u>
Transfer price based on TNMM	₹ <u>7,150</u>

Selection of Transfer Pricing Method

Rule 10C of the Indian Income Tax Rules, 1962 states that:

In selecting a most appropriate method, the following factors shall be taken into account namely,

- (a) The nature and class of the international transaction.

- (b) The class or classes of Associated Enterprises entering into the transaction and the functions performed by them taking into account assets employed or to be employed and risks assumed by such enterprises.
- (c) The availability, coverage and reliability of data necessary for application of the method.
- (d) The degree of comparability existing between the international transaction and the uncontrolled transaction and between the enterprises entering into such transactions.
- (e) The extent to which reliable and accurate adjustments can be made to account for differences, if any, between the international transaction and the comparable uncontrolled transactions or between the enterprises entering into such transactions.
- (f) The nature, extent and reliability of assumptions required to be made in the application of a method.

The starting point to select the most appropriate method is the functional analysis which is necessary regardless of what transfer pricing method is selected. Each method may require a deeper analysis focusing on aspects relating to various methods. The functional analysis helps to:

- Identify and understand the intra-group transactions;
- Have a basis for comparability;
- Determine any necessary adjustments to the comparables;
- Check the accuracy of the method selected; and
- Over time, to consider adaptation of the policy if the functions, risks or assets have been modified.

Functional analysis also forms part of the documentation. The major components of a functional analysis are:

- 1. Identification of Functions Performed : For the purpose of determining comparability, functions of the entities play an important role.*
- 2. Identification of Risk Undertaken : A risk-bearing party should have a chance of higher earnings than a non-risk bearing party, and will incur the expenses and perhaps related loss if and when risk materializes.*
- 3. Identification of Assets used or contributed : The functional analysis must identify and distinguish tangible assets and intangible assets as this is very important for functional analysis.*

The functional analysis provides answers to identify which functions risks and assets are attributable to the various related parties. In some cases one company may perform one function but the cost thereof is incurred/ paid by the other party to the transaction. The functional analysis could emphasize that situation. The functional analysis includes reference to the industry specifics, the contractual terms of the transaction, the economics circumstances and the business strategies. A checklist with columns for each related party and if needed for the comparable parties could be used to summarize the functional analysis and give a quick idea of

which party performs each relevant function, uses what assets and bears which risk. But this short-cut overview should not be used by tax auditors to count the number of enumerated functions, risks and assets in order to determine the arm's length compensation. It should be used to consider the relative importance of each function, risk and asset. Once the functional analysis is performed and the functionality of the entity as regards the transactions subject to review (or the entity as a whole) has been completed, it can be determined what transfer pricing method is most suitable to determine the arm's length price for the transactions under the review (or the operating margin for the entity under review).

There is no universally accepted method or model which describes the technique for choosing a transfer pricing method. Traditionally comparable Uncontrolled Pricing Method, Profit Split Method, Resale Price Methods are being used in transfer pricing. Other method as TNMM may also be used after the functional analysis and global practices analysis.

Reference to Transfer Pricing Officer

Section 92CA of Income Tax Act deals with Reference to Transfer Pricing Officer by assessing officer.

It provides that Assessing Officer with prior approval of Commissioner may refer the computation of Arm's Length Price in an International Transaction to transfer pricing officer if he considers it necessary or expedient to do so. On reference by Assessing officer, Transfer Pricing Officer (TPO) shall serve a notice to the Assessee requiring him to produce the evidence in support of computation made by him of Arm's Length Price in relation to an International transaction

Who is Transfer Pricing Officer (TPO)

For the purpose of Section 92CA "Transfer Pricing Officer" means a Joint Commissioner or Deputy Commissioner or Assistant Commissioner authorized by the Board to perform all or any of the functions of an Assessing Officer specified in sections 92C and 92D in respect of any person or class of persons.

Determination of Arm's Length Price by Transfer Pricing Officer

Transfer Pricing Officer after hearing the evidences, information or documents as produced by assessee and after considering such evidence as he may require on any specified points and after taking into account all relevant materials which he has gathered, shall, by order in writing, determine the arm's length price in relation to the international transaction/specified transaction and send a copy of his order to the Assessing Officer and to the assessee. On receipt of the order from Transfer Pricing officer, the Assessing Officer shall proceed to compute the total income of the assessee in conformity with the arm's length price as determined by the Transfer Pricing Officer.

Rectification of Arm's Length Price Order by Transfer Pricing Officer

If any mistake is observed which is apparent from record, the Transfer Pricing Officer may amend any order passed by him and the provisions of Section 154 w.r.t. rectification of mistake shall apply accordingly. Where any amendment is made by the Transfer Pricing Officer, he shall send a copy of his order to the Assessing Officer who shall thereafter proceed to amend the order of assessment in conformity with such order of the Transfer Pricing Officer.

Powers of Transfer Pricing Officer

1. *Power to call evidences/Information from Assessee:*

As per Section 92CA(2), the Transfer Pricing Officer may issue a notice to the Assessee and ask him to furnish records, evidences, information in support of the computation of Arm's Length Price relating to the International Transaction.

2. *Power to amend the Order made in regard to computation of Arm length price for the transaction referred to him:*

As stated earlier, if any mistake is observed which is apparent from record, the Transfer Pricing Officer may amend any order passed by him and the provisions of section 154 w.r.t. rectification of mistake shall apply accordingly

3. *Power to proceed if the report under Section 92E is not furnished for some International transactions:*

Finance Act, 2012 has inserted section 92CA(2B) in the Act which provides that w.e.f. 1st June, 2002 if the assessee has not furnished return u/s 92E and the transfer pricing officer observe International transaction or specified domestic transactions during the course of the proceedings before him, he may proceed with deeming that such transaction has been referred to him under this section 92CA provided that the provision of this section shall not empower the Assessing Officer either to assess or reassess under section 147 or pass an order enhancing the assessment or reducing a refund already made or otherwise increasing the liability of the assessee under section 154, for any assessment year, proceedings for which have been completed before the 1st day of July, 2012

4. *Power to proceed into the cases not referred to him:*

As per amendment made by Finance Act, 2011 the jurisdiction of the Transfer Pricing Officer shall extend to the determination of the Arm's Length Price (ALP) in respect of other international transactions which are noticed by him subsequently, in the course of proceedings before him. These international transactions would be in addition to the international transactions referred to the TPO by the Assessing Officer

5. *Power to exercise all of the following powers specified in Sections 131(1)(a) to 131(1)(d) or 133(6) or 133A of Income Tax Act:*

Power u/s 131(1)(a) to 131(1)(d)

TPO have the same powers as are vested in a Court under the Code of Civil Procedure, 1908 (5 of 1908), when trying a suit in respect of the following matters, namely:—

- (a) discovery and inspection;
- (b) enforcing the attendance of any person, including any officer of a banking company and examining him on oath;
- (c) compelling the production of books of account and other documents; and
- (d) Issuing commissions.

Power u/s 133(6)

Under Section 133(6), TPO may require any person, including a banking company or any officer thereof, to furnish information in relation to such points or matters, or to furnish statements of accounts and affairs verified in the manner specified by him giving information in relation to such points or matters as his opinion will be useful for, or relevant to, any enquiry or proceeding under this Act.

Power u/s 133A - Power of Survey

Finance Act, 2011 has made an amendment which provides for the power of Survey to TPO through introduction of Section 133A. In course of the proceedings, a TPO may carry out the survey as per section 133A of Income Tax Act.

Advance Pricing Agreement

As per Section 92CC of Income Tax Act, 1961, w.e.f. 1st July, 2012, the Central Board of Direct Taxes (Board), with the approval of the Central Government, may enter into an Advance Price Agreement with any person, determining the arm's length price or specifying the manner in which arm's length price is to be determined, in relation to an international transaction to be entered into by that person.

Advance Pricing Agreement (APA) is an agreement between a taxpayer and a taxing authority(Board) on an appropriate transfer pricing methodology for fixing the arm's length price for a set of transactions over a fixed period of time in future. Importance of APA may be understood with the fact that in financial year 2011-2012, addition of about ₹ 40,000 crore income has been proposed by Transfer pricing officers.

Calculation of Arm's Length Price under Advance Pricing Agreement

Arm's Length Price under Advance Pricing Agreement shall be calculated as per method enumerated in section 92C (1) or any other method with such adjustment and variation as may be necessary and expedient so to do.

Section 92 C (1) of Income Tax Act prescribes that the arm's length price in relation to an international transaction shall be determined by any of the following methods, being the most appropriate method, having regard to the nature of transaction or class of transaction or class of associated persons or functions performed by such persons or such other relevant factors as the Board may prescribe (see rule 10B) namely:—

- (a) Comparable uncontrolled price method;
- (b) Resale price method;
- (c) Cost plus method;
- (d) Profit split method;
- (e) Transactional net margin method;
- (f) Such other method as may be prescribed by the Board.

Notwithstanding anything contained in Section 92C or Section 92CA, if the Advance Pricing Agreement has been entered between an assessee and Board in respect of one international transaction, the arm's length price will be calculated as per the provisions of Advance Pricing Agreement.

Validity of Advance Pricing Agreement

The Advance Pricing Agreement shall be valid for a period as specified in the Advance Pricing Agreement. However, this period will not be more than 5 consecutive years.

Bindingness of Advance Pricing Agreement

Advance Pricing Agreement shall be binding on:

- (a) the person in whose case, and in respect of the transaction in relation to which, the agreement has been entered into; and
- (b) on the Commissioner, and the income-tax authorities subordinate to him, in respect of the said person and the said transaction

However the advance pricing agreement shall not be binding if there is a change in law or facts having bearing on the agreement so entered.

Declaring an Advance Pricing Agreement *void ab initio*

The Board may, with the approval of the Central Government, by an order, declare an agreement to be void ab initio, if it finds that the agreement has been obtained by the person by fraud or misrepresentation of facts.

Effect of declaring an Advance Pricing Agreement *void ab initio*

If an agreement is declared *void ab initio* —

- (a) All the provisions of the Act shall apply to the person as if such agreement had never been entered into; and
- (b) Notwithstanding anything contained in the Act, for the purpose of computing any period of limitation under this Act, the period beginning with the date of such agreement and ending on the date of order for declaring an Advance Pricing Agreement *void ab initio* shall be excluded. Provided that where immediately after the exclusion of the aforesaid period, the period of limitation, referred to in any provision of this Act, is less than sixty days, such remaining period shall be extended to sixty days and the aforesaid period of limitation shall be deemed to be extended accordingly.

Procedure and Scheme of Advance Pricing Agreement

The Board may, for the purposes of this section, prescribe a scheme specifying therein the manner, form, procedure and any other matter generally in respect of the Advance Pricing Agreement. Where an application is made by a person for entering into Advance Pricing Agreement, the proceeding shall be deemed to be pending in the case of the person for the purposes of the Act.

Filing of Modified return for any assessment year relevant to a previous year to which APA applies

As per Section 92CD of Income Tax Act, 1961, w.e.f. 1st July, 2012 notwithstanding anything to the contrary contained in Section 139, where any person has entered into an agreement and prior to the date of entering into the agreement, any return of income has been furnished under the provisions of Section 139 for any assessment year relevant to a previous year to which such agreement applies, such person shall furnish, within a period of three months from the end of the month in which the said agreement was entered into, a modified return in accordance with and limited to the agreement. Save as otherwise provided in Section 92CD, if modified return is furnished under Section 139, all other provision of the Act shall apply accordingly.

Thus, Section 92CD provides an opportunity to taxpayer to avoid the litigation even for the years for which return has already been filed.

Reassessment of Total Income in the cases where Modified return has been filed but the Assessment/Reassessment proceedings have been completed before the expiry of period allowed for furnishing of modified return

As per Section 92CD(3), if the assessment or reassessment proceedings for an assessment year relevant to a previous year to which the agreement applies have been completed before the expiry of period allowed for furnishing of modified return under Section 92CD, the Assessing Officer shall, in a case where modified return is filed under this Section, proceed to assess or reassess or recompute the total income of the relevant assessment year having regard to and in accordance with the agreement.

Application of APA in the pending assessment or reassessment for an assessment year relevant to the previous year to which the agreement applies and modified return has been filed under Section 92 CD.

Where the assessment or reassessment proceedings for an assessment year relevant to the previous year to which the agreement applies are pending on the date of filing of modified return in accordance with the provisions of sub-section (1), the Assessing Officer shall proceed to complete the assessment or reassessment proceedings in accordance with the agreement taking into consideration the modified return so furnished.

Extension of Limitation Period in the cases where modified return is filed under Section 92CD

As per Section 92CD (5), notwithstanding anything contained in Section 153 or Section 153B or Section 144C—

- (a) The order of assessment, reassessment or recomputation of total income under Section 92CD (3) shall be passed within a period of one year from the end of the financial year in which the modified return under sub-section (1) is furnished;
- (b) The period of limitation as provided in Section 153 or Section 153B or Section 144C for completion of pending assessment or reassessment

proceedings referred to Section 92CD(4) shall be extended by a period of twelve months.

This may be observed from above provision that Advance Pricing Agreement, although styled as "advance" agreements, may be a good arm in the resolution of transfer pricing issues pending from prior years—and in some cases it can provide an effective means for resolving existing transfer pricing audits or adjustments.

By virtue of Advance Pricing Agreement, the taxpayer is assured about the Tax Liability arising out of International transaction. No surprises or challenges will arise if the agreement is followed. The scope of certainty includes tax treatment of covered transactions as to amount and characterization, elimination of potential penalties for substantial tax understatement and a limitation of record-keeping requirements.

Transfer Pricing – Documentation

The legal framework for maintenance of information and documentation by a taxpayer is provided in Section 92D of Income Tax Act, 1961 which lays down that every person who enters into an international transaction with an associated enterprise shall maintain prescribed information and documents. The various types of information and documents to be maintained in respect of an international transaction, the associated enterprise and the transfer pricing method used are prescribed in Rule 10D of the Income Tax Rules, as under:

- (a) A description of the ownership structure of the enterprise and details of shares or other ownership interest held therein by other enterprises;
- (b) A profile of the multinational group of which the assessee enterprises i.e. taxpayer is a part and the name, address, legal status and country of tax residence of each of the enterprises comprised in the group with whom international transactions have been made by the taxpayer and the ownership linkages among them;
- (c) A broad description of the business of the taxpayer and the industry in which it operates and the business of the associated enterprises;
- (d) The nature, terms and prices of international transaction entered into with each associated enterprise, details of property transferred or services provided and the quantum and the value of each such transaction or class of such transaction;
- (e) A description of the functions performed, risks assumed and assets employed or to be employed by the taxpayer and by the associated enterprise involved in the international transaction;
- (f) A record of the economic and market analysis, forecasts, budgets or any other financial estimates prepared by the taxpayer for its business as a whole or separately for each division or product which may have a bearing on the international transaction entered into by the taxpayer;
- (g) A record of uncontrolled transactions taken into account for analysing their comparability with the international transaction entered into, including a record of the nature, terms and conditions relating to any uncontrolled

transaction with third parties which may be relevant to the pricing of the international transactions;

- (h) A record of the analysis performed to evaluate comparability of uncontrolled transactions with the relevant international transaction;
- (i) A description of the methods considered for determining the arm's length price in relation to each international transaction or class of transaction, the method selected as the most appropriate method along with explanations as to why such method was so selected, and how such method was applied in each case;
- (j) A record of the actual working carried out for determining the arm's length price, including details of the comparable data and financial information used in applying the most appropriate method and adjustments, if any, which were made to account for differences between the international transaction and the comparable uncontrolled transactions or between the enterprises entering into such transaction;
- (k) The assumptions, policies and price negotiations if any which have critically affected the determination of the arm's length price;
- (l) Details of the adjustments, if any made to the transfer price to align it with arm's length price determined under these rules and consequent adjustment made to the total income for tax purposes;
- (m) Any other information, data or document, including information or data relating to the associated enterprise, which may be relevant for determination of the arm's length price.

Rule 10D also prescribes that the above information is to be supported by authentic documents which may include the following:

- (a) Official publications, reports, studies and data bases of the government of the country of residence of the associated enterprise or of any other country;
- (b) Reports of market research studies carried out and technical publications of institutions of national or international repute;
- (c) Publications relating to prices including stock exchange and commodity market quotations;
- (d) Published accounts and financial statements relating to the business of the associated enterprises;
- (e) Agreements and contracts entered into with associated enterprises or with unrelated enterprises in respect of transaction similar to the international transactions;
- (f) Letters and other correspondence documenting terms negotiated between the taxpayer and associated enterprise;
- (g) Documents normally issued in connection with various transaction under the accounting practices followed.

Burden or Proof

It is noteworthy that the information and documentation requirements referred to above are linked to the burden of proof laid on the taxpayer to prove that the transfer price adopted is in accordance with the arm's length principle. One of the conditions to be fulfilled for discharging this burden by the taxpayer is maintenance of prescribed information and documents in respect of an international transaction entered into with a associated enterprise. A default in maintaining information and documents in accordance with the rules is one of the conditions which may trigger a transfer pricing audit under Section 92C(3). Any default in respect of the documentation requirement may also attract penalty of a sum equal to two percent of the value of the international transaction (Sec 271AA).

Submission of Documents with the Tax Authorities

There is no reference in the provisions included either in the Income Tax Act or the Income Tax Rules about any requirement to submit the prescribed information and documents at the stage of initial compliance in the form of submission of report under Section 92E. All that Section 92E requires is that the concerned taxpayer shall obtain a Report from an Accountant in the prescribed form (Form 3CEB) and submit the Report by the specified date.

Form 3CEB contains a certificate from the Accountant that in his opinion proper information and documents as prescribed have been maintained by the taxpayer. Rule 10D requires that the information and document maintained should be contemporaneous as far as possible and should exist latest by the specified date for filing the report under Section 92E. Section 92D also provides that information and documentation may be requisitioned by the Assessing Officer or the Appellate Commissioner on a notice of thirty days which period may be extended by another period of 30 days.

Non Applicability of Documentation Requirement

Although the law has prescribed no monetary limit in respect of international transaction covered by the transfer pricing requirements, an exception is provided in para 2 of Rule 10D in respect of the maintenance of information and document requirement in respect of international transactions not exceeding ₹ 100 Lakhs . It is provided that the above requirement will not apply to such transactions. However, the concerned taxpayer may be required to substantiate on the basis of available material that the income arising from the international transaction is computed in accordance with the arm's length rule.

Retention Period of Documents kept under Rule 10D

The prescribed information and documents are required to be maintained for a period of six years from the end of the relevant Assessment years thus the information and documents are required to be maintained for a period of eight years. Rule 10D absolves a taxpayer entering into an international transaction which continues to have effect over more than one year from maintaining separate set of documents for each year. However separate documents are required for each year if there is any significant change in the terms and conditions of the international transaction which have a bearing on the transfer price.

Transfer Pricing – Penalty for Contravention

Contravention of Transfer Pricing provisions as contained in Chapter X of the Income tax Act, 1961 may invite hefty penalties. The details of penalties under different sections of Income tax Act, 1961 are as follows :-

A. Penalty for concealment of income or for furnishing inaccurate particulars of such income under Section 271(1)(c)

If the Assessing Officer or Commissioner (Appeals) or the Commissioner in the course of any proceedings under this Act, is satisfied that any person has concealed the particulars of his income or furnished inaccurate particulars of such income, he may direct that such person shall pay by way of penalty in addition to tax, if any, payable by him, a sum which shall not be less than, but which shall not exceed three times, the amount of tax sought to be evaded by reason of the concealment of particulars of his income or the furnishing of inaccurate particulars of such income.

Explanation 7 to Section 271(1)(c) - Where in the case of an assessee who has entered into an international transaction defined in section 92B, any amount is added or disallowed in computing the total income under sub-section (4) of section 92C, then, the amount so added or disallowed shall, for the purposes of clause (c) of this sub-section, be deemed to represent the income in respect of which particulars have been concealed or inaccurate particulars have been furnished, unless the assessee proves to the satisfaction of the Assessing Officer or the Commissioner (Appeals) or the Commissioner that the price charged or paid in such transaction was computed in accordance with the provisions contained in section 92C and in the manner prescribed under that Section, in good faith and with due diligence.

B. Penalty for failure to furnish information or document - Section 271G

As per Section 271G of Income Tax Act, If any person who has entered into an international transaction fails to furnish any such information or document as required by sub-section (3) of section 92D, the Assessing Officer or the Commissioner (Appeals) may direct that such person shall pay, by way of penalty, a sum equal to two per cent of the value of the international transaction for each such failure.

C. Penalty for failure to keep and maintain information and document in respect of International transaction - Section 271AA

Without prejudice to the provisions of Section 271 or Section 271BA, if any person in respect of an International transaction Fails to keep and maintain any such information and document as required by sub-section (1) or sub-section (2) of Section 92D.

The Assessing Officer or Commissioner (Appeals) may direct that such person shall pay, by way of penalty, a sum equal to two per cent of the value of each international transaction entered into by such person.

D. Penalty for failure to furnish report under Section 92E - Section 271BA

If any person fails to furnish a report from an accountant as required by Section 92E, the Assessing Officer may direct that such person shall pay, by way of penalty, a sum of one hundred thousand rupees.

E. Penalty for failure to answer questions, sign statements, furnish information, returns or statements etc. - Section 272A

If any person,—

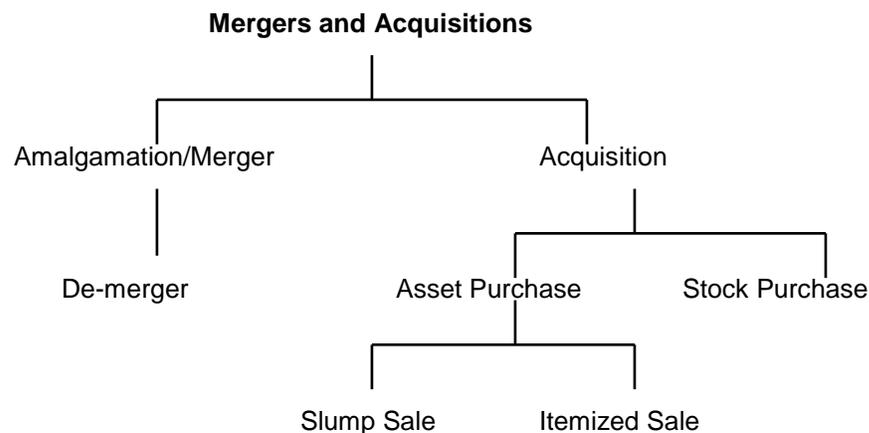
- (a) being legally bound to state the truth of any matter touching the subject of his assessment, refuses to answer any question put to him by an income-tax authority in the exercise of its powers under this Act; or
- (b) refuses to sign any statement made by him in the course of any proceedings under this Act, which an income-tax authority may legally require him to sign; or
- (c) to whom a summons is issued under sub-section (1) of Section 131 either to attend to give evidence or produce books of account or other documents at a certain place and time omits to attend or produce books of account or documents at the place or time, he shall pay, by way of penalty, a sum of ten thousand rupees for each such default or failure.

10.9 TAXATION ASPECT OF INTERNATIONAL MERGER AND ACQUISITIONS

The law relating to transfer pricing in India is still in its infancy. Some decisions recently from the Tribunal and High Court have clarified some issues. However, by its very nature the law to procedures on the subject are found to be long drawn and complicated. It will take time before the concepts get cleared and stabilized.

With the Globalised economy, trans-border merger and acquisitions are now common phenomena specially in advanced and developing companies. India is catching up with the world trend with respect to transactions involving Mergers and Acquisitions and cross border acquisitions and mergers are getting popular.

In India Mergers and Acquisitions take place in the following ways:



Definition of 'Amalgamation' under the Income Tax Act, 1961

Section 2(1B). It is defined thus : “Amalgamation” in relation to companies means, the merger of one or more companies with another company or the merger of two or more companies to form one company”

Provided:

- All assets to be transferred from amalgamating company to the amalgamated company.
- All liabilities including contingent liabilities to be transferred from amalgamating company to amalgamated company.
- Shareholders holding at least 3/4th in value of shares of the amalgamating company should become shareholders of the amalgamated company.

10.10 ACQUISITION

No definition of 'Acquisition has been given of the term in the Income Tax Act. However, as per Section 2(1B) of the Income Tax Act amalgamation is not include acquisition. The relevant portion in section 2(1B) reads thus :

“Amalgamation”, in relation to companies, means the merger of one or more companies with another company or the merger of two or more companies to form one company (the company or companies which so merge being referred to as the amalgamating company or companies and the company with which they merge or which is formed as a result of the merger, as the amalgamated company) in such a manner that—

- (i) All the property of the amalgamating company or companies immediately before the amalgamation becomes the property of the amalgamated company by virtue of the amalgamation;
- (ii) All the liabilities of the amalgamating company or companies immediately before the amalgamation become the liabilities of the amalgamated company by virtue of the amalgamation;
- (iii) Shareholders holding not less than [three-fourths] in value of the shares in the amalgamating company or companies (other than shares already held therein immediately before the amalgamation by; or by a nominee for, the amalgamated company or its subsidiary) become shareholders of the amalgamated company by virtue of the amalgamation.

Otherwise than as a result of the acquisition of the property of one company by another company pursuant to the purchase of such property by the other company or as a result of the distribution of such property to the other company after the winding up of the first mentioned company.

Benefits for amalgamation under the Income Tax Act, 1961

Amalgamations have been given certain benefits under the Income Tax Act. These are :

- (i) No tax is to be charged on capital gain arising on :

Scheme of Amalgamation

- (i) **Section 47(vi)** : Any transfer, in a scheme of amalgamation, of a capital asset by the amalgamating company to the amalgamated company is an Indian Company.

Transfer of Capital Asset → From Amalgamating Company → To Indian Amalgamated Company.

- (ii) **Section 47(via)** : Any transfer, in a scheme of amalgamation, of a capital asset being a share or shares held in an Indian company, by the amalgamating foreign company to the amalgamated foreign company, if—

- (a) At least twenty-five per cent of the shareholders of the amalgamating foreign company continue to remain shareholders of the amalgamated foreign company; and
- (b) Such transfer does not attract tax on capital gains in the country, in which the amalgamating company is incorporated;

- (iii) **Section 47(vii)**: Any transfer by a shareholder, in a scheme of amalgamation, of a capital asset being a share or shares held by him in the amalgamating company if—

- (a) The transfer is made in consideration of the allotment to him of any share or shares in the amalgamated company; and
- (b) The amalgamated company is an Indian company.

Transfer of Capital Assets → From a shareholders for consideration of allotment to him of any share(s) → In the Indian amalgamated company.

- (iv) **Section 79**: Carry forward and set-off losses in case of certain companies : Notwithstanding anything contained in this Chapter, where a change in shareholding has taken place in a previous year in the case of a company, not being a company in which the public are substantially interested, no loss incurred in any year prior to the previous year shall be carried forward and set off against the income of the previous year unless—

- (a) On the last day of the previous year the shares of the company carrying not less than fifty-one per cent of the voting power were beneficially held by persons who beneficially held by persons who beneficially held shares of the company carrying not less than fifty-one per cent of the voting power on the last day of the year or years in which the loss was incurred.

Provided that nothing contained in this section shall apply to a case where a change in the said voting power takes place in a previous year consequent upon the death of a shareholder or on account of transfer of shares by way of gift to any relative of the shareholder making such gift

Provided further that nothing contained in this sections hall apply to any change in the shareholding of an Indian company which is a subsidiary

of a foreign company as a result of amalgamation or demerger of a foreign company subject to the condition that fifty-one per cent shareholders of the amalgamating or degermed foreign company continue to be the shareholders of the amalgamated or the resulting foreign company.

- (v) **Section 72A(2)** : Provisions relating to carry forward and set-off accumulated loss and unabsorbed depreciation allowance in amalgamation or demerger, etc.

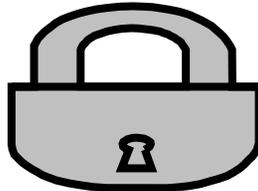
Notwithstanding anything contained in sub-section (1), the accumulated loss shall not be set off or carried forward and the unabsorbed depreciation shall not be allowed in the assessment of the amalgamated company unless—

- (a) The amalgamating company—
- (i) has been engaged in the business, in which the accumulated loss occurred or depreciation remains unabsorbed, for three or more years;
 - (ii) has held continuously as on the date of the amalgamation at least three-fourths of the book value of fixed assets held by it two years prior to the date of amalgamation.
- (b) The amalgamated company—
- (i) holds continuously for a minimum period of five years from the date of amalgamation at least three-fourths of the book value of fixed assts of the amalgamating company acquired in a scheme of amalgamation.
 - (ii) continues the business of the amalgamating company for a minimum period of five years from the date of amalgamation;
 - (iii) fulfills such other conditions as may be prescribed to ensure the revival of the business of the amalgamating company or to ensure that the amalgamation is for genuine business purpose.
 - (iv) No tax exemption is provided under the Income Tax Act, 1961, in case of amalgamation of an Indian Company into a foreign company wherein the resultant amalgamated company is a foreign company.
 - (v) In U.S.A., Section 367 of their Internal Revenue Code (IRC) exempts U.S. corporate entity in some cases relating to taxation aspect relating to merger and acquisitions.
 - (vi) In E.U., Deferral of Tax on Capital Gains on the Capital Assets transferred and shares received in consideration in qualifying transaction. But such relief can be claimed only when the assets become connected with local Permanent Establishment of the Amalgamating Company. Apart from this, domestic law will be effective in connection with carry forward of losses. But after formation of CFC requires and formulation of Bilateral Treaties, the incidence of tax evasion and tax-avoidance has been minimal.

LESSON ROUND UP

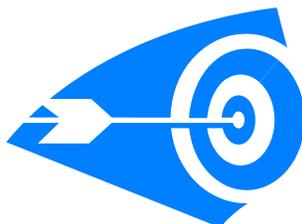
This Chapter includes :

- Taxation aspect regarding residency issues.
- Various sources of income in relation to Income Tax Act
- Tax havens
- Domestic Tax Reforms
- Definition of CFC
- The Sub Part F Regime
- Resident of Contracting State..
- Double Tax Avoidance
- Transfer pricing
- International merger and acquisitions

SELF-TEST QUESTIONS

1. What are tax havens in relation to International Taxation?
 2. What is Transfer pricing? Explain it in relation to the provisions of the Income Tax Act 1961.
 3. What do you mean by Subpart F and CFC?
 4. Discuss briefly the Subpart F income and operating rules.
 5. What are the relevant provisions regarding to DTAA in India?
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STUDY XI
ADVANCE RULING AND TAX PLANNING



LEARNING OBJECTIVES

The objective of this Chapter is to cover following topics/concepts :

- Concept of Advance ruling, authority for advance rulings and salient features
- Its power and procedure
- Who can seek Advance Ruling, the application for advance ruling and procedure on receipt of application.
- Applicability of advance ruling

11.1 CONCEPT OF ADVANCE RULING

The concept of advance rulings under the Act was introduced by the Finance Act, 1993, Chapter XIX-B of the Act, which deals with advance rulings, came into force with effect from 1.6.1993. Under the scheme, the power of giving advance rulings has been entrusted to an independent adjudicatory body designated, as Authority for Advance Rulings (AAR). Accordingly, a high level body headed by a retired judge of the Supreme Court has been set-up. There are two members in the body. AAR is empowered to give rulings, which are binding both on the Income-tax Department and the applicant. The procedure prescribed is simple, inexpensive, expeditious and authoritative.

The term advance ruling has been defined in section 245N of the Act. “Advance ruling” means,

- (i) a determination by the Authority in relation to a transaction which has been undertaken or is proposed to be undertaken by **a non-resident applicant;**
or
- (ii) a determination by the Authority in relation to the **tax liability of a non-resident** arising out of a transaction which has been undertaken or is proposed to be undertaken by **a resident applicant with such non-resident,**
- (iii) a determination or decision by the Authority in respect of an **issue** relating to **computation of total income** which is **pending** before any **income-tax authority** or the **Appellate Tribunal.**

Further, advance ruling may be determined for both the question of law or fact.

11.1.1 WHO CAN SEEK ADVANCE RULING?

As per Section 245N(b) of the Income Tax Act, the advance ruling under the income-tax act could be sought by :

- (a) A non-resident;
- (b) Resident having transactions with non-residents.
- (c) Specified categories of residents.
 - I. A non-resident is defined in section 2(30) of the Income Tax Act as a person who is not a 'resident' [and for the purposes of Section 92, 93 and 168, includes a person who is not ordinarily resident within the meaning of Clause 6 of Section 6.]
 - II. A resident has been defined in section 2(42) of the Income Tax Act as a person who is resident in India within the meaning of Section 6.
 - III. A person has been defined in section 2(31) of the Income Tax Act as including :
 - (i) an individual
 - (ii) a Hindu undivided family
 - (iii) a company
 - (iv) a firm
 - (v) an association of persons or a body of individuals, whether incorporated or not.
 - (vi) a local authority; and
 - (vii) every artificial juridical person, not falling within any of the preceding sub-clauses.

11.1.2 AUTHORITY FOR ADVANCE RULING: CONCEPT OF ADVANCE RULING AND CREATION OF AUTHORITY FOR ADVANCE RULING

Under the scheme, as now enacted, it has been decided to entrust the power of giving advance rulings to an independent adjudicatory body and to ensure further that the procedure is simple, inexpensive, expeditious and authoritative. Accordingly, a high level body headed by

- a Chairman, retired Judge of the Supreme Court
- an officer of the Indian Legal Revenue Service who is qualified to be a member of CBDT
- an officer of the Indian Legal Service who is, or is qualified to be, an Additional secretary to the Government of India

has been set up which is empowered to issue rulings which are binding both on the Income-tax Department and the applicant.. This Authority is a quasi-judicial body having full powers of a civil court under the Income-tax Act to give its rulings in respect of specific questions of law or fact.

All the three Members of the Authority function as a body in disposing off the applications before them. However, section 245P makes it clear that no proceeding before the Authority, or the pronouncement of advance ruling by the Authority, shall be questioned or shall be invalid on the ground merely of the existence of any vacancy or defect in the Constitution of the Authority.

Under Rule 27 of the AAR Procedure Rules, 1996 the proceedings of the Authority shall be conducted in the following manner :

- (1) When one or both of the members of the Authority other than Chairman is unable to discharge his functions owing to absence, illness or any other cause or in the event of occurrence of any vacancy or vacancies in the office of the members and the case cannot be adjourned for any reason, the Chairman alone or the Chairman and the remaining member may function as the Authority.
- (2) Subject to the provisions of sub-rule (3), in case there is difference of opinion among the members hearing an application the opinion of the majority of members shall prevail and orders of the Authority shall be expressed in terms of the views of the majority but any member dissenting from the majority view may record his reasons separately.
- (3) Where the Chairman and one other member having a case under sub-rule (1) are divided in their opinions, the opinion of the Chairman shall prevail.

11.1.3 APPLICATION FOR ADVANCE RULING

An applicant shall make an application in such form and in such manner as may be prescribed, stating the question on which the advance ruling is sought. The application shall be made in quadruplicate and be accompanied by a fee of two thousand five hundred rupees. An applicant may withdraw an application within thirty days from the date of the application.

(a) FORMS

The application may be withdrawn within 30 days from the date of the application.

34C Applicable for a non-resident applicant.

34D Applicable for a resident having transactions with a non-resident

34E Applicable for the notified residents.

(b) PROCEDURE ON RECEIPT OF APPLICATION

On receipt of an application, the Authority shall forward one copy of the application to the Commissioner having jurisdiction over the case of the applicant and, if considered necessary by the Authority, relevant records can also be obtained from the Commissioner. In cases where the applicants are not existing assesses, some times it becomes difficult to determine as to which Commissioner would have jurisdiction over the case of the applicant. In such cases, the Central Board of Direct Taxes (CBDT) is to be requested under Rule 13(1) of the Procedure Rules to

designate a Commissioner in respect of an applicant within two weeks. The designated Commissioner is also called upon to offer his comments on the contents of the application under Rule 13(2) of the Procedure Rules, which are considered by the Authority along with the statement of facts and submissions of the applicant.

Section 254R(2) of the Income Tax Act provides that the Authority may, after examining the application and the records called for, either 'allow' or 'reject' the application. The word 'allow' has been used synonymously with 'admit'. In other words, after examining the records, the Authority either admits or rejects the application. In case Authority has admitted the application, it is empowered to collect or received additional material and it will examine all the material thus available to it at the time of hearing and pronouncing a ruling on the application. In case the application has been rejected then an opportunity of being heard must be given to the assessee.

The authority shall pass the ruling in writing within six months of the receipt of application and the copy of the order thereof, shall be sent to the commissioner and assessee.

(c) SALIENT FEATURES

(a) Available for Income-tax, Customs and Central Excise:

The benefit of advance ruling is available under the Income Tax Act, 1961, Central Excise Act, 1944 and Customs Act, 1962.

(b) Must relate to a transaction entered into or proposed to be entered into by the applicant.

(c) Questions on which ruling can be sought :

(i) Even though the word used in the definition is singular namely "question", it is clear that there can be more than one question in one application. This has been made amply clear by Column No.8 of the Form of application for obtaining an advance ruling (Form No.34C).

(ii) a question can be both of law or fact, pertaining to the income tax liability of the non-resident qua the transaction undertaken or proposed to be undertaken.

(iii) The questions may be on points of law as well as on facts or could be mixed questions of law and facts. There should be so drafted that each question is capable of an answer. This may need breaking-up of complex questions into two or more simple questions.

(iv) The questions should arise out of the statement of facts given with the application. No ruling will be given on a purely hypothetical question. Question not specified in the application can be raised during the course of hearing. Normally a question is not allowed to be amended but in deserving cases AAR may allow amendment of one or more questions.

(v) Subject to the limitations to be presently referred to, the question may relate to any aspect of the non-resident's liability including international

aspects and aspects governed by double tax avoidance agreements. The questions may even cover aspects of allied laws that may have a bearing on tax liability such as the law of contracts, the law of trusts etc., but the question must have a direct bearing, on and nexus with the interpretation of the Indian Income-tax Act.

11.1.4 POWERS OF THE AUTHORITY

Section 245U deals with the Powers of the Authority. Sub-section (1) provides that for the purpose of exercising its powers, the Authority shall have all the powers of a Civil Court under the Code of Civil Procedure, 1908 (5 of 1908) as are referred to in Section 131 of the Income-tax Act, when trying a suit in respect of the following matters, namely :

- (a) Discovery and inspection;
- (b) Enforcing the attendance of any person, including any officer of a banking company and examining him on oath;
- (c) Compelling the production of books of account and other documents; and
- (d) Issuing commissions.

Under sub-section (2) the Authority shall be deemed to be a Civil Court for the purposes of Section 195 of the Code of Criminal Procedure. Section 195 deals with 'Prosecution for contempt of lawful authority of public servants, for offences against public justice and for offences relating to documents given in evidence'. But it would not be deemed to be a Court for the purposes of Chapter XXVI of the Code of Criminal Procedure which deals with 'Provisions as to offences affecting the administration of justice'. Further, every proceeding before the authority shall be deemed to be a judicial proceeding within the meaning of Sections 193 and 228, and for the purpose of Section 196 of the Indian Penal Code. Section 193 deals with punishment for false evidence and the same is reproduced below :

"193 : Whoever intentionally gives false evidence in any stage of a judicial proceeding, or fabricates false evidence for the purpose of being used in any stage of a judicial proceeding, shall be punished with imprisonment of either description for a term which may extend to seven years, and shall also be liable to fine; and whoever intentionally gives or fabricates false evidence in any other case, shall be punished with imprisonment of either description for a term which may extend to three years, and shall also be liable to fine."

Section 228 of the Indian Penal Code deals with intentional insult or interruption to public servant sitting in judicial proceeding and the same is reproduced as below:

"228 : Whoever intentionally offers any insult, or causes any interruption to any public servant, while such public servant is sitting in any stage of a judicial proceeding, shall be punished with simple imprisonment for a term which may extend to six months, or with fine which may extend to one thousand rupees, or with both".

Section 196 of the I.P.C. deals with 'using evidence known to be false' and is set-out as follows :

"196 : Whoever corruptly uses or attempts to use as true or genuine evidence any evidence which he knows to be false or fabricated, shall be punished in the same manner as if he gave or fabricated false evidence."

Thus, the authority would have all the powers of the Civil Court for the purposes of dealing with intentional insult, false evidence etc.

11.1.5 APPLICABILITY OF ADVANCE RULING (SECTION 245-S)

The advance ruling pronounced by the Authority under Section 245R shall be binding only :

- (a) On the applicant who had sought it;*
- (b) In respect of the transactions in relation to which the ruling had been sought; and*
- (c) On the Commissioner, and the income-tax authorities subordinate to him, in respect of the applicant and the said transaction."*

The effect of the ruling is, understandably, stated to be confined to the applicant who has sought it as well as the Commissioner and the income-tax authority subordinate to him having jurisdiction over the case and that too only in relation to transaction for which advance ruling was sought. It may, however, be stated that the Authority generally follows the ruling in other cases on materially similar facts and, most certainly in other cases raising the same question of law, if any, which it has decided. The rule here is different from the position in other countries where either the taxpayer or the revenue or both are at liberty to accept the ruling or not.

Question precluded:

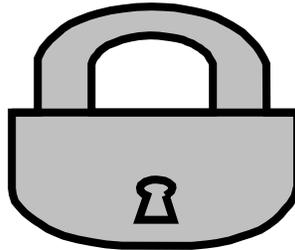
Under Section 254R, certain restrictions have been imposed on the admissibility of an application, if the question concerned is pending before other authorities. According to it, the authority shall not allow an application where the question raised by the non-resident applicant (or a resident applicant having transaction with a non-resident) is already pending before any income-tax authority or appellate tribunal or any court of law. However, exception has been provided in cases of resident applicants falling in sub-clause (iii) of Clause (b) of Section 245N in cases of pending before income tax authorities or the Tribunal. Further, the authority shall not allow the application where the question raised in it:

- (i) Involves determination of fair market value of any property; or
- (ii) It relates to a transaction or issue which is designed *prima facie* for the avoidance of income-tax.

LESSON ROUND UP

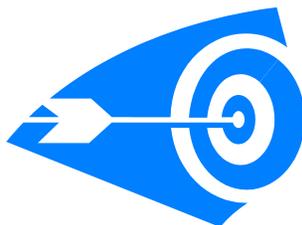
This Chapter includes :

- Authority for advance rulings
- Its power and procedure
- Applicability of advance ruling
- Application for advance ruling and procedure on receipt of application.
- Tax planning and special provisions relating to certain incomes of non-resident corporate assessee.

SELF-TEST QUESTIONS

1. What do mean by authority of advance ruling with regard to international taxation in India.
 2. Discuss the powers of authority of advance ruling in India.
 3. Discuss briefly the tax planning with regard to non-residence corporate entities.
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STUDY XII
TAXATION OF INBOUND TRANSACTIONS



LEARNING OBJECTIVES

The objective of this Chapter is to cover following topics/concepts :

- Inbound and Outbound transaction
- Taxation of passive investments
- Inbound investment strategies
- Entry options for foreign entities in India
- Foreign Direct Investment
- Automatic route
- Government approvals
- Reforms in the foreign investment regime
- Taxation of capital gains & losses
- Taxation of Income from property
- Branch profit taxation

In India, Financial Institutional Investors (FII's) can invest in Government securities as well as private securities subject to guidelines prescribed by the RBI and SEBI. The pecuniary limits regarding such investments have been liberalized consequent to market reforms initiated by the Government of India. Regarding income from royalties and technical services non-resident corporate entities or NRIs are assessable for incomes that may accrue or arise in India under the provision of Section 9 of the Income Tax Act. A foreign company planning to set-up business operations in India has the following entry options:

- (a) As a company incorporated under the Companies Act, 1956 through Joint Ventures; or wholly owned subsidiaries
- (b) As an office of a foreign entity like Liaison Office/Representative Office/Project Office/Branch Office etc.

12.1 WHAT IS INBOUND & OUTBOUND TRANSACTION

Inbound and outbound transactions are the broad categories of Cross border transaction. Inbound transaction refers to a transaction through which a foreigner or foreign entity earns income in India. For example Mercedes-Benz UK Limited having its registered office at UK sells its product in India. Hence Mercedes- Benz would be

considered in inbound category. Cross border tax issues related to inbound transaction can include UK withholding tax, transfer pricing, branch profits tax, DTAA etc.

Outbound transaction refers to a transaction through which an Indian or Indian entity earns income outside India. For instance Tata Motors is an Indian Automobile company which sells its product in Italy, Poland etc. thus Tata Motors would be considered outbound category. Cross border related to tax issues can include foreign withholding taxes, transfer pricing, foreign tax credit, subpart F income, DTAA etc,

In this chapter we will discuss the inbound transaction only and the outbound transaction will be covered in Chapter 13.

12.2 TAXATION OF PASSIVE INVESTMENTS

These have been group earlier in Chapter X as under:

- (i) Dividend income;
- (ii) Interest on securities;
- (iii) Income from royalties;
- (iv) Income from technical services;
- (v) Rental income;
- (vi) Income from transfer of short-term capital asset.

Dividend Income received by a foreign company or non-resident or FII shall be taxable @20% (other the dividend referred in section 115-O). Domestic companies distributing dividends are required to pay dividend distribution tax under section 115-O of the Income Tax Act for the Assessment Year 2013-14 the tax rate is 15% + Surcharge @ 5% + Education Cess @ 2% + Additional Education Cess @ 1% i.e., 16.60875. Dividend has been defined under Section 2(22) of the Income Tax Act in an inclusive way. Section 56(2)(i) of the Income Tax Act treats such income as income from other sources.

In India a Foreign Institutional Investor (FII) can invest in Government securities as well as private securities subject to guidelines prescribed by the RBI and the SEBI. The monetary limits regarding investments from FIIs have been liberalized consequent market reforms initiated by the Government of India. Interest on securities are treated as income from other sources under the Act while section 56(2)(id). Regarding income from royalties and technical services, non-resident corporate entities and others are assessed for incomes that may accrue or arise in India under the provision of Section 9 of the Income Tax Act.

12.3 INBOUND INVESTMENT STRATEGIES

With liberalization of the Indian economy from 1991-92 various avenues have been opened for the financial sectors for the enough fiscal incentives announced by the Finance Ministry in union budgets each year clearly indicate that, India has embarked on market reforms measures and as a result FIIs are attracted to make Investments in India in large numbers.

Under Government policy the manufacturing sector got the maximum tax incentives by which FII's can invest upto 100% through automatic route. And likewise in telecommunication, banking insurance sectors, etc. investments can be made by FIIs, ranging from 26% to 74%.

In order to add to the liquidity in the market through the utilization of international capital markets, policy Government permits issue of GDR's FCB's, etc.

Tax advantage is also admissible through bilateral treaty agreements with various countries; India has entered Double Taxation Avoidance Agreement (DTAA) with large number of countries like U.K., Singapore, Mauritius, etc. Section 91 of the Income Tax Act, 1961 tax relief's in situations where there is no DTAA as mentioned in earlier discussion.

India as a further measure has exempted dividend income from tax, Government of India has also reduced limitations on FII's investment in Government Bonds and Corporate Bonds and has also reduced SLR (Statutory Liquidity Ratio) requirements.

FII's desire to invest in tax jurisdictions where they can minimize their tax obligations. Hence facilities to lower taxes are provided through tax treaties. For example, under Indo-Singapore DTAA, Economic Co-operation Agreement (ECA), etc. Regarding capital gains incomes accruing to a Singaporean Company in respect of sale of shares of a domestic company are exempt from tax in India. The thrust of the FII's, thus is to get tax exemption of their earnings (dividends or consideration for sale of securities or other income) which is comparatively profitable considering other competitive jurisdictions. Some of the popular DTAA agreements relating to inbound investment are with countries like Mauritius, Cyprus, Singapore, etc. Apart from the above, there are tax holiday schemes under the Income Tax Act for some special destinations. The following are some provisions of Income Tax Act dealing with the matters relating to the tax concessions which are open to FIIs also.

Section 80HH of the Income Tax Act provides tax incentives provided to the investors who set-up industrial undertakings and hotel business in backward areas. Similarly under Section 80IA of the Act, incentives provided with respect to profit and gains from industrial undertakings or enterprises engaged in infrastructure development. Now foreign enterprises can join the local, entities (which are registered in India) as an 'associate enterprise' or wholly owned subsidiary of the local company.

Section 112(1) of the Act provides that where the total income of the assessee includes any income, arising from the transfer of a long-term Capital Asset which is chargeable under the head 'Capital Gains' then the tax payable by the assessee on the total income shall be aggregate of the; in the case of a non-resident (not being a company) or a foreign company :

- (i) The amount of income tax payable on the total income as reduced by the amount of such long-term capital gains; had the total income as so reduced been its total income; and
- (ii) The amount of Income Tax calculated on such long-term capital gains @ 10%.

Under Section 115A of the Act, where the total income of:

- (a) a foreign company includes any income by way of :
 - (i) Dividends other than dividends referred in Section 115-O i.e., where the Company has paid dividend distribution tax, Income Tax shall be payable on income by way of dividend is @20%.
 - (ii) The tax payable on interest received from Government or an Indian concern on monies borrowed on debt incurred by the Government or the Indian concern in foreign currency shall also be @ 20%.

The rate of tax on royalties and technical fees are :

- (i) For royalty or technical fees received through an agreement before 01.06.1997 @30% (rate of Income Tax)
- (ii) From 1.06.1997 to 31.05.2005 - @ 20% (rate of Income Tax) and after 31.05.2005 it is @ 10% (rate of Income Tax).

Section 115AB prescribes the rate of tax in respect of Income of an assessee, which is an overseas financial organization (as defined) in the Explanation to the section), from limits purchased in foreign currency or capital gains arising from their transfer. The general rate mentioned is 10%

Sections 115AC and 115ACA relates to taxation of income from bonds or global Depository Receipts purchased in foreign currency. Section 115AD relates to tax on income of FII's from securities or capital gains arising from their transfer.

12.4 ENTRY OPTIONS FOR FOREIGN COMPANIES

A foreign company planning to set up business operations in India has the following entry options:

- As an incorporated entity by getting incorporated under the Companies Act, 1956 or through Joint Ventures; as Wholly Owned Subsidiaries
- As an office of a foreign entity like a Liaison Office/ Representative Office/Project Office/Branch Office

Entry routes can be through technical collaboration or through financial collaboration.

Such investments are made either under automatic route or approval route. Investment under automatic route involves post facto approval of RBI for the investments made and the Investments under approval route require prior approval of FIPB.

Foreign Direct Investment in India is allowed on automatic route in almost all sectors except

- Proposals that require an industrial licence and cases where foreign investment is more than 24% in the equity capital of units manufacturing items reserved for the small scale industries.
- Proposals in which the foreign collaborator has a previous venture/tie-up in India.

- Proposals relating to acquisition of shares in an existing Indian company in favour of a Foreign/Non-Resident Indian (NRI)/Overseas Corporate Body (OCB) investor; and
- Proposals falling outside notified sectoral policy/caps or under sectors in which FDI is not permitted etc

12.5 FOREIGN DIRECT INVESTMENT

Government wishes to facilitate foreign direct investment (FDI) and investment from Non-Resident Indians (NRIs) including Overseas Corporate Bodies (OCBs), that are predominantly owned by them, to complement and supplement domestic investment. Investment and returns are freely repatriable, except where the approval is subject to specific conditions such as lock-in period on original investment, dividend cap, foreign exchange neutrality, etc. as per the notified sectoral policy. The condition of dividend balancing that was applicable to FDI in 22 specified consumer goods, industries stands withdrawn for dividends declared after 14th July 2000.

Foreign direct investment is freely allowed in all sectors including the services sector, except where the existing and notified sectoral policy does not permit FDI beyond a ceiling. FDI for virtually all items/activities can be brought in through the Automatic Route under powers delegated to the Reserve Bank of India (RBI), and for the remaining items/activities through Government approval. Government approvals are accorded on the recommendation of the Foreign Investment Promotion Board (FIPB).

12.6 AUTOMATIC ROUTE

(a) New Ventures

All items/activities for FDI/NRI/OCB investment up to 100% fall under the Automatic Route except those which require an industrial licence; foreign collaborator has previous venture/tie-up in India; proposals relating to acquisition of shares in an existing Indian Company in favour of a foreign/NRI/OCB investor; and proposals falling outside the notified sectoral policy/caps or under sectors in which FDI is not permitted whenever any investor chooses to make an application to the FIPB and not to avail of the automatic route, he or she may do so. Investment in public sector units as also for EOU/EPZ/EHTP/STP units would also qualify for the Automatic Route. Investment under Automatic Route are to be governed by the notified sectoral policy and equity caps and RBI ensures compliance of the same. The National Industrial Classification (NIC) 1987 is applicable for description of activities and classification for all matters relating to FDI/NRI/OCB investment.

(b) Foreign Investment in Existing Companies

Besides new companies, automatic route for FDI/NRI/OCB investment is also available to the existing companies proposing to induct foreign equity. For existing companies with an expansion programme, the additional requirements are that (i) the increase in equity level must result from the expansion of the equity base of the existing company without the acquisition of existing shares by NRI/OCB/foreign investors, (ii) the money to be remitted should be in foreign currency and (iii)

proposed expansion programme should be in the sector(s) under automatic route. Otherwise, the proposal needs Government approval through the FIPB. For this purpose the proposal must be supported by a Board Resolution of the existing Indian company.

For existing companies without an expansion programme, the additional requirements for eligibility for automatic approval are that (i) they are engaged in the industries under automatic route, (ii) the increase in equity level must be from expansion of the equity base and (iii) the foreign equity must be in foreign currency.

The earlier SEBI requirement, applicable to public limited companies that shares allotted on preferential basis are not transferable in any manner for a period of 5 years from the date of their allotment, has now been modified to the extent that not more than 20 per cent of the entire contribution brought in by promoter cumulatively in public or preferential issue shall be locked-in.

The automatic route for FDI and/or technology collaboration is not available to those who have or had any previous joint venture or technology transfer/trade mark agreement in the same field in India.

Equity participation by international financial institutions such as ADB, IFC, CDC, DEG, etc. in domestic companies is permitted through automatic route to SEBI/RBI regulations and sector specific cap on FDI.

In a major drive to simplify procedures for foreign direct investment under the "automatic route", RBI has given permission to Indian Companies to accept investment under this route without obtaining prior approval from RBI. Investors are required to notify the Regional Office concerned of the RBI of receipt of inward remittances within 30 days of such receipt and file required documentation within 30 days of issue of shares to Foreign Investors. This facility is available to NRI/OCB investment also.

12.7 GOVERNMENT APPROVAL

The Government approval for NRI/OCB through the FIPB route is necessary for following categories:

- (i) All proposals that require an Industrial Licence which includes (1) the item requiring an Industrial Licence under the Industries (Development & Regulation) Act, 1951; (2) foreign investment being more than 24 per cent in the equity capital of units manufacturing items reserved for small scale industries; and (3) all items which require an Industrial Licence in terms of the locational policy notified by Government under the New Industrial Policy of 1991.
- (ii) All proposals in which the foreign collaborator has a previous venture/tie up in India. The modalities prescribed in Press Note No. 18 dated 14.12.1998 of 1998 Series, are applicable to such cases. However, this is not applicable to investment made by multilateral financial institutions such as ADB, IFC, CDC, DEG, etc. as also investment made in IT sector.
- (iii) All proposals relating to acquisition of shares in an existing Indian company in favour of a foreign/NRI/OCB investor.

- (iv) All proposals falling outside notified sectoral policy/caps or under sectors in which FDI is not permitted.

RBI has granted general permission under Foreign Exchange Management Act (FEMA) in respect of proposals approved by the Government. Indian companies getting foreign investment approval through FIPB route do not require any further clearance from RBI for the purpose of receiving inward remittance and issues of shares to the foreign investors. Such companies are, however, required to notify the Regional Office concerned of the RBI of receipt of inward remittances within 30 days of such receipt and to file the required documents with the concerned Regional Offices of the RBI within 30 days after issue of shares to the foreign investors.

12.8 REFORMS IN THE FOREIGN INVESTMENT REGIME

Since export growth depends on the existence of a strong production base in thrust sectors, which could expand to meet further growth needs, the stimulus in such thrust areas has been provided by streamlining the procedures for foreign investment. The Foreign Investment Promotion Board (FIPB) has been revamped to make the rules and regulations pertaining to foreign investment more transport. The first-ever guidelines for approving FDI by the FIPB have been announced to expedite approval of foreign investment in areas not covered under automatic approval. Priority areas for allowing 100% foreign equity was spelt out. An expanded list of 46 industries eligible for automatic approval up to 51% foreign equity, three industries relating to mining activity eligible for automatic approval upto 50% foreign equity and another set of nine industries eligible for 74% foreign equity was announced by the Government. The limit on holdings by individual foreign institutional investors (FIIs) in a company has been raised from 5% to 10% of the company's shares, while the aggregate limit has been increased from 24% to 30%. FIIs were also allowed to invest in non-listed companies. It is no longer necessary for automatic approvals by the Reserve Bank of India (RBI) that the amount of foreign equity should cover the foreign exchange requirements for import of capital goods needed for the project. To impart flexibility in sourcing of technology imports, technology transfer has been delinked from equity investment.

12.8.1 NEW PRESS NOTE CONCERNING FDI

Recently, the Government of India issued Press Note 7 (2008 series) laying down policy on Foreign Direct Investment. The press note provides in a consolidated form, policy prevailing at present concerning FDI. It states about FIPB approval route and the automatic route. All such sectors which are not covered under the FIPB approved route shall be under the automatic route except where FDI is completely prohibited. In prohibited areas investment can be made with the approval of the Government through FIPB.

(a) Prohibited Areas: According to this Press Note, FDI is prohibited in the following areas :

- Retail trading (except single brand retail trading).
- Atomic energy
- Lottery business
- Gambling and betting

- Business of Chit Fund
- Nidhi Company
- Trading in Transferable Development Rights
- Activity/sector not open to private sector investment.

(b) *Prior Government Approval:* In the following situations prior Government approval would be necessary.

- Where provisions of Press Note 1 (2005 series) are attracted.
- Where more than 24% foreign equity is proposed to be inducted for manufacturing of items reserved for small sector.

(c) *Approval Route:* There are sectors where prior approval of FIPB is necessary before any FDI is committed. Such sectors have been detailed in Table No.1 of the Press Note including applicable cases on investments and the conditions subject to which approval shall be granted.

12.8.2 WITHHOLDING TAX FOR NRIs AND FOREIGN COMPANIES

Withholding Tax Rates for payments made to Non-Residents are determined by the Finance Act passed by the Parliament annually. The current rates are:

- Investment Income – 20%
- Interest - 20% of Gross Amount
- Royalties - 10% where the agreement is made on or after 1st June, 2005.
- Technical Services - 20%
- Income by way long-term Capital gains refund to in section 115E – 10%
- Income by way of short-term capital gains referred to in Section 11A -15%
- On other incomes by way of long-term capital gains (holding long-term Gains referred to in clause (33), (36) and (38) of Section 10 - 20%
- Any other Services –like winning from lotteries - 30%.

The above rates are general and in respect of the countries with which India does not have a Double Taxation Avoidance Agreement (DTAA).

The Organization for European Economic Cooperation (OEEC) worked from 1948 for the preparation of a draft convention for the avoidance of Double Taxation with respect to taxes on income and capital. This work was later on taken over by the Organization for Economic Cooperation and Development (OECD) set-up in 1961 in which all the developed countries were members. The developed countries have followed the drafts so prepared in 1963 and revised in 1977 in their agreements with other developed countries. The 1977 OECD Model has again been revised as the Model Tax Convention on Income and Capital (Paris, 1992) in the light of the studies conducted on “International Tax Avoidance and Evasion”, “Thin Capitalization”, “Taxation of Income derived from Entertainment, Artistic and Sporting Activities”, and other issues during the intervening years.

After the Second World War, many of the countries in Asia and Africa gained independence and started improving their economies. The desirability of promoting greater inflow of foreign investment to developing countries on conditions which are

politically acceptable, besides being economically and socially beneficial, has been frequently affirmed in resolutions of the General Assembly, the UN Economic and Social Council and the UN Conference on Trade and Development. It was recognized that foreign private capital flows and investments play an important complementary role in the economic development process, particularly through—

- (a) The transfer of resources, managerial and administrative expertise and technology to the developing countries.
- (b) The expansion of manufacturing capacity and employment in the developing countries; and
- (c) The establishment of export of markets.

In 1968, the Secretary-General of the United Nations set up an ad hoc group of experts on tax treaties between developed and developing countries. This group consisted of tax officials and experts from the following countries, appointed in their personal capacity : Argentina, Chile, France, German Democratic Republic; Ghana, India, Israel, Japan, Netherlands, Norway, Pakistan, Philippines, Sudan, Switzerland, Tunisia, Turkey, United Kingdom of Great Britain and United States of America, Sri Lanka was added in 1972 and Brazil in 1973.

This group of experts drafted the final Model Convention which was published by the United Nations in 1980 along with commentaries. This Model Convention of the United Nations, called UN draft, has now become the standard format for the tax treaties which are being concluded between the developed and developing nations. The agreements concluded by India in the recent years have also been based on this UN Model, with suitable modifications to reflect the Indian laws and the laws of the countries with which the agreements are concluded.

12.9 TAX ON INCOME OF FOREIGN INSTITUTIONAL INVESTORS FROM SECURITIES OR CAPITAL GAINS ARISING FROM THEIR TRANSFER (SECTION 115AD)

A reference about the section has already been made earlier. Some salient aspects concerning the section are mentioned hereinafter :

The Section provides as under :

- (1) Where the total income of a Foreign Institutional Investor includes—
 - (a) Income (other than income by way of dividends referred to in Section 115-O) received in respect of securities (other than unit referred in Section 115AB); or
 - (b) Income by way of short-term or long-term capital gains arising from the transfer of such securities.

The Income-tax payable shall be the aggregate of—

- (i) the amount of income-tax calculated on the income in respect of securities referred to in Clause (a), if any, included in the total income, at the rate of twenty per cent;
- (ii) the amount of income-tax calculated on the income by way of short-term

capital gains referred to in Clause (b), if any, included in the total income, at the rate of thirty per cent :

Provided that the amount of income-tax calculated on the income by way of short-term capital gains referred to in Section 111A shall be at the rate of ten per cent.

- (iii) the amount of income-tax calculated on the income by way of long-term capital gains referred to in clause (b), if any, included in the total income, at the rate of ten per cent; and
- (iv) the amount of income-tax with which the Foreign Institutional Investor would have been chargeable had its total income been reduced by the amount of income referred to in clause (a) and clause (b);

(2) Where the gross total income of the Foreign Institutional Investor—

- (a) consists only of income in respect of securities referred to in Clause (a) of sub-section (1), no deduction shall be allowed to it under Sections 28 to 44C or Clause (i) or Clause (iii) of Section 57 or under Chapter VI-A;
- (b) includes any income referred to in Clause (a) or Clause (b) of sub-section (1), the gross total income shall be reduced by the amount of such income and the deduction under Chapter VI-A shall be allowed as if the gross total income as so reduced, were the gross total income of the Foreign Institutional Investor.

(3) Nothing contained in the first and second provisions to Section 48 shall apply for the computation of capital gains arising out of the transfer of securities referred to in Clause (b) of Sub-section (1).

Explanation—for the purposes of this section :

- (a) the expression “Foreign Institutional Investor” means such investor as the Central Government may, by notification in the Official Gazette, specify in this behalf.
- (b) the expression “securities” shall have the meaning assigned to it in Clause (h) of Section 2 of the Securities Contracts (Regulation) Act, 1956 (42 of 1956).

These are the tax incentives in India which FII's can use in to planning their investment strategies. How they should approach the Indian Market and under what form is a business decision which they have to take considering various tax incentives and provisions prevalent here. A tax planner like company secretary can advise them so that they have minimal tax liability on the transactions, they enter upon.

12.10 PROPERTY AND CAPITAL GAIN TAX (RELATING TO SECURITIES)

It is an ad-valorem tax, payable by a property owner to the authorities for possessing a immovable property. Property can be transferred through sale, lease, etc.

Tax on property transfers is payable the shape of duties, levied under Stamps Act of 1899 and Registration Act, 1908. The rates of duties are stated in the schedule attached with the respective Acts.

Property under Income Tax Act, 1961 includes Land, Property (Leasehold + purchased). Deductions for house property income in the Income Tax Act, 1961, are contained in Section 24 of the Act. On transfer of property capital gains tax is payable.

12.11 LONG-TERM CAPITAL GAINS IN RESPECT OF SHARES, SECURITIES AND UNITS [SECTION 112]

If the following conditions are satisfied, then tax on long-term capital gain will be computed under Alternative A or Alternative B as given below :

Conditions: The following conditions should be satisfied :

- | | |
|--------------------|--|
| <i>Condition 1</i> | The taxpayer is an individual, HUF, company or any other person (may be resident or non-resident). |
| <i>Condition 2</i> | The asset is a long-term capital asset |
| <i>Condition 3</i> | The long-term capital asset is :
(a) a security listed in any recognized stock exchange in India; or
(b) a unit of UTI or a mutual fund (whether listed in a recognized stock exchange or not); or
(c) zero coupon bonds. |

Section 2(h), "securities" include—(i) shares, scrips, stocks, bonds, debentures, debenture stock or other marketable securities of a like nature in or of any incorporated company or other body corporate; (ii) Government securities; (iii) such other instruments as may be declared by the Central Government to be securities; and (iv) rights or interest in securities.

Tax Computation – If the capital asset which is transferred is equity shares or units of equity oriented mutual fund and the transaction is subject to securities transaction tax, the long-term capital gain is not chargeable to tax. In other case, if the conditions given in box are satisfied, tax shall be computed as follows (i.e., Alternative A or Alternative B whichever is lower :

<i>Alternative A</i>	<i>Alternative B</i>
1. Find out sale consideration	Find out sale consideration
2. Deduct: Indexed cost of acquisition/ improvement and expenses on transfer.	Deduct: Cost of acquisition/ improvement and expenses on transfer.
3. The balancing amount [i.e., (1) – (2) is long-term capital gain	The balancing amount [i.e., (1) – (2) is long-term capital gain
4. 20 per cent (+SC+EC+SHEC) of (3) is the amount of tax liability.	10 per cent (+SC+EC+SHEC) of (3) is the amount of tax liability.

If several transactions have taken place by way of sale of shares, etc., the assessee can avail the benefit of indexation in a few transactions and avail the 10 per cent tax rate on the remaining transactions—*Devinder Prakash Kalra v. CIT* [2005] 97 ITJ (Delhi) 372.

The taxpayer has an option in respect of each transaction to pay tax under Alternative A or Alternative B whichever is lower. It is not possible to state when Alternative A or B is better. This will depend on the facts and circumstances in different cases. However, in the case of transfer of listed bonus shares, listed debentures, listed bonds and zero coupon bonds, Alternative B will be better as compared to Alternative A.

Short-term Capital Gain/Taxation (Section 111A) : The provisions of Section 111A are given below :

Conditions – Section 111A is applicable if the following conditions are satisfied—

- (i) The assessee is an individual, HUF, firm, company or any other person.
- (ii) During the previous year, he has generated short-term capital gain on transfer of equity shares or units in equity-oriented mutual fund.
- (iii) Such transaction is chargeable to securities transaction tax at the time of transfer.

Consequences—If the above conditions are satisfied, short-term capital gain is taxable at the rate of 10 per cent (+SC+BC+SHEC).

No deduction is available under Sections 80C to 80U from the above-noted short-term capital gains.

Exemption limit in some cases [Proviso to Section 111A] – The proviso to Section 111A gives relief as under :

Conditions: The relief is available if the following conditions are satisfied :

- (i) The taxpayer is a resident individual or a resident Hindu undivided family. He or it may be ordinarily resident or not ordinarily resident.
- (ii) Taxable income minus short-term capital gain [given in para] is less than the amount of exemption limit ₹2,40,000 in the case of resident senior citizen (60 years but below 80 years), ₹5,00,000 in case of very senior citizen (80 years or above), ₹2,00,000 in the case of any other individual or HUF (for the Assessment Year 2013-14).

Relief – If the aforesaid conditions are satisfied, the following shall be deducted from such short-term capital gains :

Exemption limit – (Net income or taxable income – Such short-term capital gain)

After deducting the aforesaid amount, the balancing amount of such short-term capital gain is chargeable to tax.

12.12 BRANCH PROFIT TAXATION

'Stamp Duty' and Registration Fees are chargeable on the Charter document, i.e., the Memorandum and Articles of Association of the Company. These taxes are approximately 2% of the stated authorized share capital of the company.

There are no other significant taxes. There is no Special Branch Office Tax. A Branch Office of a Foreign Company is treated as Permanent Establishment (P/E)

and the foreign company is taxable on the profits of the foreign company that are attributable to the branch. The taxable profit of a local branch would be calculated in the same manner as the profits of a domestic company but taxable at a rate prescribed for foreign companies.

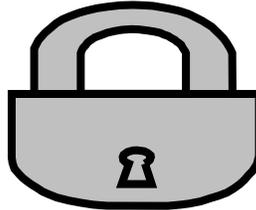
LESSON ROUND UP



The chapter includes:

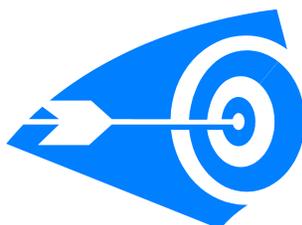
- Taxation of passive investments
- Inbound Investment Strategies
- Entry options foreign entities willing to invest in India
- Reforms in the Foreign Investment Regime
- Foreign Direct Investment
- Capital gains & losses
- Property taxation
- Branch profit taxation

SELF-TEST QUESTIONS



1. What is Passive Investment Taxation?
2. Discuss briefly the entry points for an foreign entities through which they can invest in India.
3. Discuss in short the relevant provisions of the Section 115AD of the Income Tax Act.
4. What do mean by Branch Profit Taxation?
5. Explain briefly the relevant issues relating to property taxation specially involving capital gains.
6. What do you mean by withholding tax for NRIs and foreign entities?

STUDY XIII
TAXATION OF OUTBOUND TRANSACTIONS



LEARNING OBJECTIVES

The objective of this Chapter is to cover following topics/concepts :

- Foreign tax credit
- Recent case
- Tax exclusions (exemption with respect to foreign income)
- Outward Investment strategies
- PFIC's (Passive Foreign Investment Companies).

With the onset of globalization, Indian enterprises are going abroad for tax efficient jurisdictions for minimizing their tax liability. Cross country investment have a financial dimension affecting the tax base of the domestic companies. The transaction includes M&A, transfers and taking advantage of indirect foreign tax credit.

Outbound transaction refers to a transaction through which an Indian or Indian entity earns income outside India. For instance Tata Motors is an Indian Automobile company which sells its product in Italy, Poland etc. thus Tata Motors would be considered outbound category. Cross border related to tax issues can include foreign withholding taxes, transfer pricing, foreign tax credit, subpart F income, DTAA etc.

13.1 FOREIGN TAX CREDIT

Tax credit in India is generally governed by the provisions of a bilateral Double Taxation Avoidance Agreement ('DTAA' or 'the Treaty') concluded between India and the other contracting state. Further, where there is no DTAA, section 91 of the Indian Income-tax Act, 1961 ('the Act') grants unilateral relief in respect of income which has suffered tax both in India and in a country with which no DTAA exists (ie doubly taxed income)

1. Methods for availing tax credits under the DTAAs:

Broadly, a DTAA would seek to eliminate juridical double taxation through either of the following two alternative mechanisms:

- Exemption method
- Credit method

1.1 Exemption method

Under the Exemption method, the State of Residence ('State R') does not tax the income, which according to DTAA may be taxed in the State of Source ('State S').

1.2 Credit method

Under the Credit method, State R includes income from State S in the taxable total income of the tax payer and calculates its tax on the basis of such taxpayer's total income (including income from State S). It then allows a deduction from its own taxes for taxes paid in State S. The Credit method can be applied with several variations –

- Ordinary credit method,
- Underlying Tax Credit method, and
- Tax Sparing credit.

1.2.1 Ordinary credit method

Ordinary credit method refers to allowance of credit, from the tax payable in India, to the extent of tax attributable to the income that has been taxed in State S. The restriction may also be on grant of credit only in respect of income that is taxed in the overseas jurisdiction, i.e. credit would be granted qua each item of income and only if the same item of income has suffered tax in the overseas jurisdiction.

DTAAs executed by India usually follow the 'Ordinary Credit method' for elimination of double taxation, for the taxes paid by an Indian resident, either directly or by way of deduction, in the foreign country.

1.2.2 Underlying Tax Credit ('UTC') method

UTC is a method to provide relief from the doubly taxed income. UTC refers to the credit that may be given, in a Contracting State (State R), for the tax paid on the underlying profits out of which the dividend is paid by a company in the Other Contracting State (State S).

DTAAs entered into by India (like DTAAs with Mauritius, Singapore) provide for UTC in situations where an Indian company is a shareholder in a foreign company.

1.2.3 Tax Sparing credit

Some of the DTAAs contain "tax sparing" clauses, whereby, tax incentives offered by the particular foreign country are deemed to have been paid as a foreign tax for the purpose of computing the foreign tax credit granted. Essentially, tax sparing consists of granting a tax credit in a Contracting State for the amount of tax that would have been payable in the Other Contracting State ie, State S had there been no reduction or exemption under the tax regime of State S.

Few DTAAs with India contain tax sparing provisions, for eg, DTAAs executed with China, Qatar, Singapore (on certain select income streams), Kenya, Philippines, Bangladesh, Korea, Malaysia and Nepal provides tax sparing benefits.

13.2 CASE LAWS

(1) *Tata Sons Limited v. DCIT*

In case of *Tata Sons Limited v. DCIT* [ITA 4978/Mum/04], it was held that credit state taxes could be claimed under Section 91.

Foreign income-taxes not eligible for deduction under section 37(1). Despite bar in DTAA, credit for State taxes to be given under section 91 in addition to Federal taxes.

Facts of the Case:

In respect of Assessment Year 2000-01, the assessee earned profits on export of software which was eligible for deduction under section 80HHE. The assessee paid foreign income-taxes of ₹ 60 crores on the said profits in respect of which the assessee claimed tax credit under sections 90 & 91. The assessee also claimed that it was eligible for a deduction under section 37(1) in respect of the said foreign income-taxes. While the AO allowed tax credit, he denied deduction under section 37(1) on the ground that the said payment of foreign taxes was an “application of income” and that it was hit by section 40(a)(ii). On appeal, the CIT(A) upheld the claim of the assessee by following the orders of the Tribunal in the assessee’s own case & where a department’s reference under section 256(2) had been rejected the Bombay High Court. In appeal before the Tribunal the department argued that the earlier decisions of the Tribunal should not be followed as they were against the basic scheme of the Act and also that they were no longer good law in view of Explanation 1 to section 40(a)(ii) inserted by Finance Act, 2006 w.e.f. 1.4.2006.

The Plea of the department Upheld:

(i) While there are four basic methods in which relief in the home jurisdiction can be given for taxes paid in a foreign jurisdiction, sections 90 & 91 adopt the system of granting credit for the foreign taxes against the Indian taxes payable in respect of the income;

(ii) The argument that the bar of deduction in section 40(a)(ii) is not applicable to foreign taxes is no longer acceptable in view of *Lubrizol v. CIT* 187 ITR 25 (Bom) (being rendered after the lead order of the Tribunal) where it was held that foreign tax payments is an “appropriation of income” and that the words “any tax” in section 40(a)(ii) covered foreign taxes. Further, this position is clarified by Explanation 1 to section 40(a)(i) inserted by Finance Act, 2006. Accordingly, the earlier judgements of the Tribunal cannot be followed despite the fact that the department’s reference under section 256(2) was rejected by the High Court;

(iii) The claim of the assessee that it is entitled to tax credit under sections 90 & 91 in respect of the foreign taxes as well as a deduction under section 37(1) is not justified and results in a double unintended benefit. On facts, while the assessee paid US Federal Income-tax @ 35% of ₹ 35 crores and claimed deduction under section 37(1) which resulted in tax advantage of ₹ 13 crores being 38.5% of this amount, it also claimed tax credit of ₹ 35 crores against its Indian income-tax liability despite the

fact that the profits were not taxed in India owing to deduction under section 80HHE. The result is that for a payment of US taxes of ₹ 35.01 crores, the assessee claimed tax relief of ₹ 48.49 crores in India. Even if tax credit was denied in cases where section 80HHE was eligible (as done by the CIT (A)), the assessee would still get an effective advantage of 38.5% if it was granted a deduction under section 37(1). This results in incongruity;

(iv) The argument that if deduction under section 37(1) is not granted, credit for foreign taxes should be granted under section 90 even in respect of income eligible for deduction under section 80HHE is not acceptable because this would be contrary to the language of the DTAA and result in an assessee getting refund of US taxes if he had no tax liability in India.

(v) The argument that sections 90 & 91 are confined to USA Federal taxes and not to USA State taxes and that therefore the bar in section 40(a)(ii) does not apply to USA State taxes is not acceptable because any payment of income-tax is an application of income as held in Inder Singh Gill 47 ITR 284. Further, the scheme of sections 90 & 91 does not discriminate between Federal taxes and State taxes and though the India-USA DTAA confines the credit only to Federal taxes, the assessee will be entitled to relief under section 91 in respect of both taxes as that will be more beneficial to the assessee *vis-à-vis* tax credit under DTAA. Consequently, the bar against deduction in section 40(a)(ii) will apply to USA State taxes as well though the assessee will be entitled to credit in respect of USA State taxes.

(2) Wipro Ltd. v. DCIT-ITA Nos.895 & 896/Bang/03 and 881&882/Bang/03 dated 21st June 2005

In this case the Bangalore Tribunal as held that foreign taxes in respect of income earned abroad will be available as per the provisions of the tax treaty, irrespective of whether income is taxable in India or not provided the income is included in the return of income filed in India. The Tribunal also held that incentive provisions/deductions available should not be brushed aside on a technical consideration. Therefore, even a claim made under Section 80HHE of the Income Tax Act, 1961, in the course of assessment proceedings must be entertained. The order of the ITAT deals with various issues including computation of income under sections 10A/80-IA of the Act.

13.3 Tax Exclusions (Exemptions) with respect to foreign income

There are a variety of tax concessions available to foreign corporate entities investing in India. It includes partial tax holidays for newly established small scale industrial units, established in FTZ and 100% EOU's.

Special tax incentives provided to FII's in respect of income from securities and capital gains.

Dividends and interest on investments made by FII's are taxed at a concessional rate of 20% and long term capital gains @ 10%. Short term capital gains on sale of securities are subject to tax @30% further short term capital gain if covered under

section 111A shall be taxable @15%. Indian companies required to pay 20% tax on long term gains. However, foreign companies and non-resident non-corporate tax payers are charged at a concessional rate of 10% on long term capital gains.

These includes :

- (a) Exemptions for new industrial undertakings in FTZ's
- (b) Deductions in case of royalties and fees for technical services earned by foreign nationals in India
- (c) Section 80HHE, provides that for deductions of all profits derived from the export of computer Software from the total income of the tax payer. This concession is available also to the Indian companies.

Apart from this, sections 112 and 111A of the Income tax Act deals with the provisions relating to capital gains taxation.

Special tax concessions is made available EEC investors under section 10(23BBB) of the Income Tax Act 1961.

Section 196D of the Act provides for withholding tax @20% from income derived by FII's from securities. The deduction must be made either when the income is credited to the payee's account, when the payment is made in cash or when a cheque or draft is issued, whichever is earlier. Surcharge and Education cess/ Secondary and Higher Education cess would be applicable as per schedule rates.

There are other incentives for tax holidays specially relating to investments made in new industrial undertakings in under-developed areas. Moreover tax holiday facilities available for power generating sector and investment in building infrastructures.

There is also provision for deduction for capital expenditure for scientific research under section 35 of the Act. The government of India from time to time issue notifications and circulars relating to granting of concessions to corporate or non-corporate entities under sections 35, 10(6), etc., of the Act.

To encourage venture capital financing , section 10(23F) of the act provides an income tax exemption for all dividends and long term capital gains of a venture capital fund or a venture capital company from investments made by way of equity shares in venture capital undertakings. To obtain this exemption, venture capital fund or company must obtain approval from the prescribed authority and satisfy the prescribed conditions.

13.4 OUTWARD INVESTMENT STRATEGIES

With the on set of globalization Indian enterprises are going abroad for tax efficient jurisdiction for minimizing their tax liability cross country investment have a financial dimension effecting the tax base of the domestic companies.

<i>The following is the tax slab applicable for the Assessment Year 2012-13.</i>		<i>Rates</i>
<i>A. In case of domestic company</i>		<i>30%</i>
<i>B. In case of foreign company:</i>		
<i>(i) On so much of the total income as consists of :</i>		
<i>(a) Royalties received from Government or an Indian Concern in pursuance of an agreement made by It with the Government or the Indian concern After 31st March 1961 but before 1.4.1976 or;</i>		
<i>(b) Fees for rendering technical services received Government or an Indian concern in pursuance of an agreement made by it with the Government or the Indian concern after 29.2.1964 but before 1.4.1976 and where such agreement has, in either case, been approved by the Central Government.</i>		<i>50%</i>
<i>(ii) On the balance, if any, of the total income.</i>		<i>40%</i>

13.5 SURCHARGE ON INCOME TAX (IN THE CASE OF COMPANIES)

The amount of Income-tax computed in accordance with the preceding provisions of this paragraph, or in Section 111A or Section 112 shall in case of every company, be increased by a surcharge for purposes of the Union calculated—

- (i) In the case of every domestic company at the rate of 5% of such income tax.
- (ii) In the case of every company other than domestic company @ 2%.

Now from the above statement it can be observed that, the effective rate of Income Tax is :

For the Assessment Year 2012-13 :

- (i) For Domestic Companies – 30% + Surcharge if applicable (5%) + Education Cess (3%).
i.e., $30\% + 5\%/100 \times 30 + 3/100 \times 31.5 = 32.445\%$
- (ii) For b(i) Companies – 50% + 2% + 3%
i.e., $50 + 2/100 \times 50 + 3/100 \times 51 = 52.53\%$
- (iii) For b(ii) Companies – 40 + 2% × 40 + 3% × 40.8
i.e., 42.024%.

Therefore, the corporate tax is about 32%, 53% and 42% in different cases. It is too high considering other tax jurisdictions abroad. So some Indian companies are going abroad to minimize their tax obligations to avail of lower rates of tax.

13.6 PASSIVE FOREIGN INVESTMENT COMPANY (PFIC)

A passive foreign investment company (or "PFIC") is a foreign company with predominantly investment income, or whose assets are primarily intended to generate investment income. The Internal Revenue Service in U.S.A. handles the profits of investments in PFICs differently than their domestic counterparts. So U.S. investors have different tax implications should they hold ownership of a PFIC. Unlike

the controlled foreign corporation provisions, which focus more on tax havens, the PFIC provisions focus on foreign investment structures. Classification as a PFIC occurs when 75% or more of the company's income is passive, or when more than 50% of the company's assets exist in investments earning interest, dividends, and/or capital gains.

The drawback to this tax is that natural resource exploration companies tend to be PFIC's because their main assets are the cash they are using to explore with. That cash is earning more interest than the company earns from any other business which brings them under the PFIC definition that was set up to close a tax avoidance loophole.

Tax code sections 1291 to 1297 of IRC provide the rules for U.S. tax payers who invest in passive foreign investment companies. A foreign corporation is considered a "passive foreign investment company" for these purposes if either of two tests are satisfied : The Income Test or the Asset Test.

Under the Income Test, a foreign corporation is considered a PFIC if 75 percent or more of the foreign corporation's gross income for the taxable year consist of passive income. Passive income includes dividends, interest, royalties, rents, annuities, net gains from certain commodities transactions, net foreign currency gains, income equivalent to interest, payments in lieu of dividends, income from notional contracts, and income from certain personal service contracts. Note that the active business of a licensed bank or insurance business is considered active income; similarly, certain foreign trade income and income allocated to a related person's non-passive income is also excluded.

Under the Asset Test, a foreign corporation is considered a PFIC if 50 percent of the foreign corporation's assets produce - or are held to produce - passive income. In applying the Asset Test, the fair market value of the assets is generally used (the "FMV Method"). The general exception is a foreign corporation that is not publicly-traded and is a [controlled foreign corporation], which must use the adjusted basis of its assets in applying the Asset Test (the "Basis Method"). A taxpayer may also elect to utilize the basis method, but, once this is done, may not change back to the FMV method without IRS consent.

There are two important exceptions to these rules for calculation. First, Congress has recognized that newly-formed corporations frequently hold short-term investments that may create a significant percentage of income prior to the business truly commencing. As such, in the first taxable year in which a foreign corporation has gross income (the "Start-up Year"), the company will not be considered a PFIC.

Prior to the enactment of the Constitution, the Government of India Act, 1935 provided that the Federal Legislature had no power to make laws for a Province or for any part thereof with reference to any of the matters enumerated in the Provincial Legislative List. Entry 48 of the Provincial List read "taxes on the sale of goods and on advertisements". This entry was construed to mean a power to tax the transaction on the sale of goods and in *V.M. Syed Mohamad & Co. v. State of Madras* AIR (1953), Mad. 105 it was held that the entry should be construed to mean a power to tax the transaction of sale and the power to tax the transaction carried with it the power to tax either part thereto and thus the expression 'tax on sale' in this entry was

held to mean also tax on purchase of goods. By virtue of the power so conferred under the List many of the States started taxing goods by relying on one or more ingredients of a sale, namely:

- (i) Existence of goods which form the subject matter of the sale,
- (ii) The bargain or contract which when executed, will result in passing of the property for a price,
- (iii) The payment or terms of payment of a price, and
- (iv) The passing of title in the goods.

When the Constitution was enacted, almost the same distribution of legislative powers between the Union and States came to be followed. Entry 54 of the State list gave exclusive power to the States to levy taxes on sale or purchase of goods other than newspapers. It is essential to note that the term 'purchase' was added in List II (This was not so in the Government of India Act, 1935 but as was observed in *V.M. Syed Mohamad & Company's Case*, the term 'sale' was held to include also the term 'purchase').

In exercise of the powers conferred under Entry 54 of the State List in the Constitution, many States started levying sales tax even if one of the ingredients of a sale was present in their State(s). The result was that the same goods came to be taxed by several States. For instance, on the basis of situs of the goods at the time of sale one State sustained the levy. Another State sustained the levy on the basis that the goods were actually delivered in that State; yet another State sustained the levy on the ground that the goods were actually found in that State and so on and so forth. The short contention of each State was that there existed a territorial connection (nexus) between the State and the sale, the subject matter of taxation. This nexus theory was supported by reference to various court decisions abroad. The nexus theory was sought to be vigorously enforced by reference to an income tax case - *Governor General in Council v. Raleigh Investment Company Ltd.* AIR (1944) FC 51, 15 ITR 332 (PC).

Thus, the extra territorial operation of the sales tax laws of many of the States were sought to be justified on the basis of the nexus theory. The danger of this theory was that the same transaction of sale was brought to tax by different State Governments resulting in higher burden ultimately on the consumer of goods. Under the nexus theory it was considered sufficient that there should be a territorial nexus between the taxing State and the subject of taxation and that all the ingredients of a sale like the agreement to sell, passing of title, delivery of goods, etc. need not necessarily take place within the territorial limit of the State seeking to impose the tax. This reasoning was adopted in the *State of Bombay and another v. United Motors (India) Ltd. and others* (1953) 4 STC 133 (SC); *Popatlal Shah v. State of Madras* (1953) 4 STC 1988 (SC).

Even after the enactment of Article 286 of the Constitution there were certain problems. In *State of Bombay v. United Motors (India) Limited* (1953) 4 STC 133 (SC), the Supreme Court held that Article 286(1)(a) prohibited taxation of sale or purchase involving inter-State elements by all States except the State in which the goods were actually delivered for the purpose of consumption therein and that the

effect of the Explanation was to convert inter-State transaction into intra-State transaction and to remove them from the operation of clause (2) of Article 286.

The Constitution was, therefore, amended in the year 1956 in order to clearly enunciate the law on sales tax. Accordingly, Article 286 was amended by the Constitution (6th Amendment) Act, 1956. Article 286 now reads as follows:

- “286. (1) No Law of a State shall impose or authorize the imposition of a tax on the sale or purchase of goods where such a sale or purchase takes place:
- (a) Outside the State or
 - (b) In the course of the import of the goods into or export of the goods out of the territory of India.
- (2) Parliament may by law formulate principles for determining when a sale or purchase of goods takes place in any of the ways mentioned in clause (1).
- (3) Any law of a State shall, in so far it imposes, or authorizes the imposition of, a tax on the sale or purchase of goods declared by Parliament by Law to be of special importance in inter-State trade or commerce, be subject to such restrictions and conditions in regard to the system of levy, rates and other incidents of the tax as Parliament may by law specify.”

Simultaneously, the Parliament also amended List I whereby it inserted Entry No. 92A which empowered the levy of taxes on the sale or purchase of goods other than newspapers where such sale or purchase takes place in the course of inter-State trade or commerce. The Amendment Act further amended Entry 54 in the State List (List II) whereby the States, power was confined to taxes on the sale or purchase of goods other than newspapers subject to the provisions of Entry 92A of List I. The Amendment Act further provided in Article 269 that Parliament may by law formulate principles for determining when a sale or purchase of goods takes place in course of inter-State trade or commerce.

LESSON ROUND UP



This Chapter includes:

- Matters relating to Foreign tax credit
- Foreign income exemptions
- PFIC's (Passive Foreign Investment Companies)

SELF-TEST QUESTIONS



1. What do you mean by foreign tax credit?
2. Distinguish between direct and indirect foreign tax credit.
3. What is CFC?
4. Discuss briefly transactions involving cross border merger, acquisition and transfers.
5. Explain briefly the issues involving taxation of PFIC in India.

PROFESSIONAL PROGRAMME
ADVANCED TAX LAWS AND PRACTICE

PP-ATLP/2012

TEST PAPERS

This Test Paper set contains five test papers. Test Paper 1/2012, 2/2012, 3/2012, 4/2012 and 5/2012. The maximum time allowed to attempt each test paper is 3 hours.

Students are advised to attempt atleast **one Test Paper from Test Papers 3/2012, 4/2012 and 5/2012 i.e. either Test Paper 3/2012 or Test Paper 4/2012 or Test Paper 5/2012** and send the response sheet for evaluation to make him/her eligible for Coaching Completion Certificate. However, students may, if they so desire, are encouraged to send more response sheets including Test Paper 1/2012 and 2/2012 for evaluation.

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W A R N I N G

Time and again, it is brought to our notice by the examiners evaluating response sheets that some students use unfair means in completing postal coaching by way of copying the answers of students who have successfully completed the postal coaching or from the suggested answers/study material supplied by the Institute. A few cases of impersonation by handwriting while answering the response sheets have also been brought to the Institute's notice. The Training and Educational Facilities Committee has viewed seriously such instances of using unfair means to complete postal coaching. The students are, therefore, strongly advised to write response sheets personally in their own hand-writing without copying from any original source. It is also brought to the notice of all students that use of any malpractice in undergoing postal or oral coaching is a misconduct as provided in the explanation to Regulation 27 and accordingly the studentship registration of such students is liable to be cancelled or terminated. The text of regulation 27 is reproduced below for information :

"27. Suspension and cancellation of examination results or registration

In the event of any misconduct by a registered student or a candidate enrolled for any examination conducted by the Institute, the Council or the Committee concerned may *suo motu* or on receipt of a complaint, if it is satisfied that, the misconduct is proved after such investigation as it may deem necessary and after giving such student or candidate an opportunity to state his case, suspend or debar the person from appearing in any one or more examinations, cancel his examination result, or studentship registration, or debar him from future registration as a student, as the case may be.

Explanation - Misconduct for the purpose of this regulation shall mean and include behaviour in a disorderly manner in relation to the Institute or in or near an Examination premises/centre, breach of any regulation, condition, guideline or direction laid down by the Institute, malpractices with regard to postal or oral tuition or resorting to or attempting to resort to unfair means in connection with the writing of any examination conducted by the Institute".

PROFESSIONAL PROGRAMME
ADVANCED TAX LAWS AND PRACTICE
TEST PAPER 1/2012

Time allowed: 3 hours

Maximum marks: 100

NOTE: *All Questions are compulsory.*

PART A – DIRECT TAXATION – LAW AND PRACTICE

1. (a) "Tax evasion is the result of suppression, misrepresentation, illegality and fraud". Explain. *(5 marks)*
(b) What is the meaning of 'company' under the Income Tax Act, 1961? Discuss the various categories of companies under the Act. *(10 marks)*
2. (a) Explain the provisions of MAT under the Income Tax Act, 1961. *(10 marks)*
(b) What are the factors to be taken into account for organizing a tax planning cell in a medium size company? *(5 marks)*

PART B – INDIRECT TAXATION – LAW AND PRACTICE

3. (a) What are the grounds on which remission of duty can be granted under Central Excise Rules, 2002? When should such application be submitted to the Central Excise Officer? *(5 marks)*
(b) What is special Audit under section 14AA of Central Excise Act, 1944? *(5 marks)*
(c) Distinguish between "Identical Goods" and "Similar goods" with reference to Customs Valuation Rules, 2007. *(6 marks)*
(d) Explain briefly the expression 'person-in charge' under the Customs Act, 1962. *(4 marks)*
4. (a) Explain in brief the provisions related to "Records", "Returns" and "Payment" under Central Excise Law. *(5 marks)*
(b). Explain the concept of "valuation based on transaction value" with special focus on the Central Excise Valuation Rules, 2000. *(10 marks)*
5. (a) What are the provisions made under the Customs Act, 1962 regarding control of customs over the warehoused goods? *(5 marks)*
(b) Describe the procedure of assessment and clearance of imported goods in the lights of the provisions of the Custom Laws. *(10 marks)*

PART C – INTERNATIONAL TAXATION

6. (a) What residency issues associated with the Advance Ruling? *(5 marks)*
(b) What do you understand by "uncontrolled transaction"? *(5 marks)*
(c) What are the benefits available for "amalgamation' under Income tax Act? *(10 marks)*

TEST PAPER 2/2012

Time allowed: 3 hours

Maximum marks: 100

NOTE: All Questions are compulsory.

PART A – DIRECT TAXATION – LAW AND PRACTICE

1. (a) Explain how is the residential status of a company determined under the Income Tax Act, 1961. (5 marks)
- (b) What do you understand by a company in which public is substantially interested? (5 marks)
- (c) Discuss the provisions related to 'appeal to the Supreme Court' under Section 261 of the Income Tax Act, 1961. (5 marks)
2. (a) What are the important areas of tax planning in the context of Income Tax Act, 1961. (10 marks)
- (b) Explain in brief the Appealable orders before the Appellate Tribunal. (5 marks)

PART B – INDIRECT TAXATION – LAW AND PRACTICE

3. (a) Choose the most appropriate answer from the given options in respect of the following:
 - (i) Duties of customs is levied by the Union Government vide Entry No.____ of the Union List :
 - (a) 82
 - (b) 83
 - (c) 84
 - (d) 85
 - (ii) Claim for refund of Excise Duty may be made within _____ from the relevant date :
 - (a) 6 months
 - (b) 1 year
 - (c) 2 years
 - (d) 3 years
 - (iii) Excise Duty on molasses of Khandsari Sugar Factory is payable by the_____
 - (a) Producer of molasses
 - (b) Procurer who uses molasses in manufacture of any commodity
 - (c) Either (a) or (b)
 - (d) None of the above

- (iv) The date for determination of duty and tariff valuation except for molasses shall be the rate in force on the date on which_____:
- (a) Goods are manufactured
 - (b) Goods are removed from the factory
 - (c) Goods are sold
 - (d) Excise duty is recovered from the buyer
- (v) CENVAT Return by a non-SSI unit is to be submitted under Self Assessment by_____
- (a) 10th day of the succeeding month
 - (b) 15th day of the succeeding month
 - (c) 25th day of the succeeding month
 - (d) End of the succeeding month
- (vi) Excise Duty is payable by _____;
- (a) 6th day of the following month
 - (b) 5th day of the following month, if paid electronically
 - (c) 31st day of March for the month of March
 - (d) All are correct
- (vii) Duties of customs shall be levied as per the provisions of Section_____ of Customs Act, 1962 at such rates as may be specified in Custom Tariff Act, 1975
- (a) 3
 - (b) 6
 - (c) 9
 - (d) 12
- (viii) As per Custom Valuation Rules, 2007 the landing charges shall be taken @ ___of CIF value for valuation purpose :
- (a) 1 %
 - (b) 1.125 %
 - (c) 1.5 %
 - (d) None of the above
- (xi) Rate of duty and tariff valuation of imported goods for home consumption shall be applicable as on the date on which_____:
- (a) Bill of Entry is presented
 - (b) Custom Duty is paid
 - (c) Any of the two which is most beneficial to the assessee
 - (d) None of the above

- (x) The Central Government has power to grant exemption from Custom Duty vide Section _____ of the Customs Act, 1962 :
- (a) 10
 - (b) 15
 - (c) 20
 - (d) 25 *(1 mark each)*
- (b) What is meant by “manufacture” under the Central Excise Act, 1944? Explain by giving reference to the relevant case laws. *(5 marks)*
- (c) Explain in brief the procedure of “refund” under Central Excise Law. *(5 marks)*
4. Discuss the salient features of CENVAT Credit Rules, 2004. *(10 marks)*
5. (a) Explain the Rules of Classification under the Custom Laws. *(5 marks)*
- (b) What do you understand by “ Warehousing bond” ? *(5 marks)*
- (c) Explain the provisions related to valuation under section 14 of the Customs Act and Custom Valuation Rules, 2007. *(10 marks)*

PART C – INTERNATIONAL TAXATION

6. (a) Explain the provisions related to “ Advance Ruling” in the Income Tax Act ? *(10 marks)*
- (b) Write a brief note on “Controlled Foreign Corporation (CFC)”. *(5 marks)*
- (c) How the Foreign Institutional Investors are taxed for the capital gains arising from transfer of securities ? *(5 marks)*
-

TEST PAPER 3/2012

Time allowed: 3 hours

Maximum marks: 100

NOTE: *All Questions are compulsory.*

PART A – DIRECT TAXATION – LAW AND PRACTICE

1. (a) Choose the most appropriate answer from the given options in respect of the following :
- (i) MAT Rate is _____% of book profit as per the Finance Act, 2012:
 - (a) 10
 - (b) 18
 - (c) 18.5
 - (d) 20
 - (ii) The last date for filling of income tax return u/s 139(4A) by a Charitable trust and institutions:
 - (a) 31st October of the Assessment year
 - (b) 30th July of the Assessment year
 - (c) 30th September of the Assessment year
 - (d) 31st August of the Assessment year
 - (iii) The rate of income tax on foreign company in respect of income from royalty received from the Government is _____% plus surcharge.
 - (a) 30
 - (b) 35
 - (c) 40
 - (d) 50
 - (iv) Credit of Minimum Alternate Tax (MAT) in respect of excess amount of tax paid under section 115JB could be carried forward for-
 - (a) 8 Assessment Year
 - (b) 5 Assessment Year
 - (c) 7 Assessment Year
 - (d) 10 Assessment Year
 - (v) _____ is an honest and rightful approach to the attainment of maximum benefits of the taxation laws within their framework.
 - (a) Tax Evasion
 - (b) Tax avoidance

- (c) Tax Planning
(d) Any of the above *(1 mark each)*
- (b) State, with reasons in brief, whether the following statements are correct or in correct:
- (i) Taxes on income and corporation tax are collected by the Central Government and distributed between the Union and States.
(ii) Companies formed under section 25 of the Companies Act, 1956 without any profit motive, trade, professional or similar associations become liable to tax under the Income Tax Act, 1961 under certain circumstances.
(iii) The minimum penalty for repayment of deposits in contravention of section 269T is Rs.25,000 and is imposed by the Assessing Officer.
(2 marks each)
- (c) Discuss the concept of 'deemed dividend' under section 2(22)(e)
(4 marks)
2. (a) What are the important areas of tax planning in the context of Income Tax Act, 1961. *(10 marks)*
(b) Explain in brief the Appealable orders before Commissioner (Appeals).
(5 marks)

PART B – INDIRECT TAXATION – LAW AND PRACTICE

3. (a) Choose the most appropriate answer from the given options in respect of the following:
- (i) The maximum amount of penalty leviable under section 117 of the Customs Act is rupees
(i) 1,00,000
(ii) 2,00,000
(iii) 50,000
(iv) 60,000
- (ii) Special Audit under section 14A of the Central Excise Act, 1944 can be ordered by _____:
(a) Assistant Commissioner of Central Excise
(b) Deputy Commissioner of Central Excise
(c) Either (a) or (b) with previous approval of Chief Commissioner
(d) Chief Commissioner
- (iii) Excisable goods means goods specified in the _____ to the Central Excise Tariff Act, 1985 as being subject to a duty of excise and include salt:
(a) First Schedule

- (b) Second Schedule
 - (c) First and Second Schedule
 - (d) Neither in First Schedule nor Second Schedule
- (iv) Notice for Custom Duty not levied or short levied or wrongly refunded etc can be served within:
- (a) 6 months in case import made for personal use
 - (b) 6 months in case import made by educational institute
 - (c) 6 months in case import made by hospital
 - (d) None of the above
- (v) If the imported goods are not cleared within _____ days of unloading at custom station, the custodian may sell them under permission of the proper officer :
- (a) 15
 - (b) 30
 - (c) 45
 - (d) 60
- (1 mark each)*
- (b) Rewrite the following sentences after filling-in the blank spaces with appropriate word(s)/figure(s):
- (i) HSN stands for _____
 - (ii) The form for 'bill of entry' for warehousing is printed on _____
 - (iii) Excisable goods consumed within the factory for manufacture of final product is called _____.
 - (vi) _____ of CENVAT Credit can be taken by the provider of output services on capital goods in the same financial year.
 - (v) Exempted goods means goods exempted by a notification under section _____ of the Central Excise Act, 1944:
- (1 mark each)*
- (c) What are the essential features of the CENVAT credit scheme in relation to capital goods? *(10 marks)*
4. (a) Write Short Note on:
- (i) Unjust Enrichment in Central Excise Law
 - (ii) Exempted and Nil rated goods *(5 marks each)*
- (b) Distinguish between the provisions of section 74 and 75 of the Customs Act, 1962 relating to duty drawback. *(5 marks)*
5. (a) Mr. B, an Indian resident, aged 50 years, returned to India after visiting England on 10/04/2012. He had been to England on 01/04/2012. On his way back to India he brought following goods with him-
- (i) His personal effects like cloths etc. valued at Rs.40,000;
 - (ii) 1 litre of Wine worth Rs.1,000;

(iii) A video cassette recorder worth Rs.11,000;

(iv) A microwave oven worth Rs.20,000.

What is the customs duty payable? *(5 marks)*

(b) Explain whether the following items can be included in/excluded from the transaction value under section 4 of the Central Excise Act, 1944:

(i) Collection expenses incurred in respect of empty bottles for filling aerated waters from the premises of buyers to the manufactures.

(ii) Delivery and collection charges of gas cylinders and collection of empty cylinders.

(iii) Interest notional or real accruing on deposits for sale/return of gas cylinders as well as rentals

(iv) Cash discount known at the time of clearance of goods but not availed by the customer.

(v) Value of system software in case of computers. *(2 marks each)*

PART C – INTERNATIONAL TAXATION

6. (a) Several Indian companies are migrating abroad to minimize their tax obligations and to avail of lower rates of tax. Discuss with reference to our current levels of tax on incomes. *(5 marks)*

(b) Write a brief note on “Foreign Direct Investment (FDI)”. *(5 marks)*

(c) What are the ‘tax exemptions’ available with respect to foreign income under Income tax Act. *(5 marks)*

(d) Discuss the scope of the provisions the Central Government may make under section 90(A)(1) of the Income Tax Act, 1961 in respect of an agreement between specified associations. *(5 marks)*

TEST PAPER 4/2012

Time allowed: 3 hours

Maximum marks: 100

NOTE: All Questions are compulsory.

PART A – DIRECT TAXATION – LAW AND PRACTICE

1. (a) Choose the most appropriate answer from the given options in respect of the following :
- (i) Any person discontinuing any business or profession shall give notice to the Assessing Officer under section 176(3) within_____ days thereof;
 - (a) 30 days
 - (b) 45 days
 - (c) 60 days
 - (d) No limit
 - (ii) As per section 5, the following is not included in the total income of a non-resident company-
 - (a) Income which is deemed to accrues or arises in India during the previous year.
 - (b) Income which arises or accrues outside India
 - (c) Income which accrues or arises in India during the previous year.
 - (d) Income which is received or deemed to be received in India.
 - (iii) A company is said to be resident in India in any previous year, if:
 - (a) It is an Indian Company
 - (b) The control and management is wholly situated in India
 - (c) Either it is a Indian company or the control and management is wholly situated in India
 - (d) It is both an Indian Company and the control and management is wholly situated in India.
 - (iv) Which of the following reflects the correct position regarding the binding powers of the Central Board of Direct Taxes (CBDT).
 - (a) The instructions of the CBDT are binding on the department and the assessee
 - (b) Courts are bound by the instructions of the CBDT.
 - (c) The instructions are binding on the department, but not on the assessee.
 - (d) The instructions by the CBDT may impose a burden on the assessee.
 - (v) An appeal to the High Court shall be filled within _____

of the date on which the order appealed against is received:

- (a) 60 days
 (b) 30 days
 (c) 45 days
 (d) 120 days (1 marks each)
- (b) What do you understand by "Book Profit" in the context of Minimum Alternate Tax. (5 marks)
2. (a) Discuss the factors on the basis of which tax planning is identified. (5 marks)
- (b) Compute the tax payable and penalty payable under section 271(1)(c) for assessment year 2013-14 from the following particulars:
- | | | |
|--|--------------------|-------------------|
| Return of loss submitted for Assessment year 2012-13 | (-)3,40,000 | |
| Additions made under section 143(3) | | |
| On question of fact | Rs.1,90,000 | |
| On question of law | <u>Rs.1,00,000</u> | <u>2,90,000</u> |
| Total loss assessed | | <u>(-) 50,000</u> |
- (5 marks)
3. (a) Distinguish between Tax Avoidance and Tax Evasion. (5 marks)
- (b) Explain the provisions relating to revision of assessment order prejudicial to the interest of assessee. (5 marks)

PART B - INDIRECT TAXATION – LAW AND PRACTICE

4. (a) Choose the most appropriate answer from the given options in respect of the following:
- (i) For offences committed under sections 132 to 135 of the Customs Act, 1962, a court shall take cognizance-
- (a) *Suo motu*
 (b) When it is brought to the notice of a court by anybody
 (c) With the previous sanction of the Commissioner of Customs
 (d) None of the above
- (ii) In case the goods removed during the month of March, the excise duty shall be paid by
- (a) 5th April of following month
 (b) 6th April of following month
 (c) 31st March of the same month
 (d) Any of the above
- (iii) Where the goods are thrown into the sea with a view to lighten the ship in order to prevent it from sinking is called:
- (a) Derelict
 (b) Flotsam

- (c) Wreck
(d) Jetsam
- (iv) Manufacturers, whose aggregate value of clearances in the preceeding financial year had not exceeding rupees_____ are entitled to the concession of a Small Scale Industries:
(a) 300 Lakhs
(b) 150 Lakhs
(c) 400 Lakhs
(d) 450 Lakhs
- (v) The duty paid on export shall be refunded if the goods are re-imported within _____ from the date of exportation:
(a) 3 months
(b) 6 months
(c) 1 year
(d) 2 years *(1 mark each)*
- (b) State with reasons in brief, whether the following statements are true or false:
- (i) The assessee shall himself assess the duty payable on any excisable goods except Cigarettes.
- (ii) A situation where excise duty is not payable on goods lost/ destroyed and found deficient in quantity on account of natural causes, unavoidable accidents etc. is called Rebate of duty.
- (iii) Normal price means the transaction value at which the greatest aggregate Quantity of goods is sold:
- (iv) The Superintendent of Central Excise has the power to grant remission of duty upto rupees 15,000.
- (v) The duty paid on export shall be refunded if the goods are re-imported within 6 months from the date of exportation:
(1 mark each)
- (c) Explain the meaning of "Baggage." What is the relevant date for determination of rate of duty and tariff valuation in case of a baggage?
(5 marks)
- (d) Explain the provisions of 'Remission of Duty' in relation to rule 21 of Central Excise Rules, 2002.
(5 marks)
5. (a) Write short notes on:
- (i) All Industry Rates
(ii) Brand Rates *(5 marks each)*
- (b) How is the assessable value determined when the excisable goods are not sold for delivery at the time and place of removal.
(5 marks)

6. (a) Explain the procedure for removal of goods by 100% EOU for Domestic Tariff Area. *(5 marks)*
- (b) Explain the residual method of valuation under Rule 9 of the Customs Import Valuation Rules, 2007. *(5 marks)*
- (c) Explain the provisions of section 113 of Customs Act, 1962 in respect of confiscation of improperly exported goods. What penalty is levied in respect of the same u/s 114 of the Act? *(5 marks)*

PART C – INTERNATIONAL TAXATION

7. (a) State with reasons in brief, whether the following statements are true or false:
- (i) The application filed for advance ruling may be withdrawn within 45 days from the date of the application
 - (ii) Uncontrolled transaction means a transaction between enterprises other than associated enterprise.
 - (iii) Form 34D is applicable for a non-resident applicant.
 - (iv) For Assessment Year 2013-14 the applicable surcharge on domestic companies is 7.5% if its total turnover exceeds Rs. 1crore.
 - (v) Financial Institutional Investors can invest in government securities as well as private securities subject to guidelines prescribed by the RBI. *(1 mark each)*
- (b) What do you mean by Arm's Length Price. What are the methods of calculating it. *(5 marks)*
- (c) Explain the powers of the authority for advance rulings in regard to rejection of an application and modification of an order. *(5 marks)*
- (d) Discuss the scope of the provisions the Central Government may make under section 90(A)(1) of the Income Tax Act, 1961 in respect of an agreement between specified associations. *(5 marks)*
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TEST PAPER 5/2012

Time allowed: 3 hours

Maximum marks: 100

NOTE: All Questions are compulsory.

PART A – DIRECT TAXATION – LAW AND PRACTICE

1. (a) Choose the most appropriate answer from the given options in respect of the following :
- (i) The parliament and the legislature of states shall have the concurrent powers :
 - (a) Union List
 - (b) State list
 - (c) Concurrent list
 - (d) None of the above
 - (ii) A Situation where a person tries to reduce his tax liability by deliberately suppressing the income or by inflating the expenditure showing the income lower than the actual income and restoring to various types of deliberate manipulations is known as:
 - (a) Tax Planning
 - (b) Tax Avoidance
 - (c) Tax Evasion
 - (d) All the above
 - (iii) For Carry Forward of loss under various heads the assessee shall file a return of loss under section 139(3) of Income Tax Act,1961 within the prescribed time limit except:
 - (a) Loss under head Capital gain
 - (b) Loss under head Profits and Gains from business or profession
 - (c) Loss under head House property
 - (d) All the above
 - (iv) An association of persons and body of individuals who are subject to tax audit in the immediately preceding financial year, making payment to resident contractor under section 194C-
 - (a) Are not liable to deduct tax at source
 - (b) Shall be liable to deduct tax at source
 - (c) Are liable to deduct tax at source, if the turnover during the current year exceeds Rs.60 Lakhs.
 - (d) None of above.
 - (v) “Book Profits” means the net profit as shown in the profit and loss account for the relevant previous year prepared under this sub-section as increased by;
 - (a) The provision for income tax

- (b) Proposed Dividend
 - (c) Depreciation
 - (d) All the above *(1 mark each)*
- (b) Examine whether the following are assets under the provisions of the Wealth Tax Act, 1957:
- (i) A commercial complex
 - (ii) A building occupied by the assessee for business purpose.
 - (iii) Aircrafts owned and used by the assessee for business purposes.
 - (iv) Land owned by the assessee situated outside a municipality but within a notified area.
 - (v) Jewellery, bullion and utensils made of precious metals. *(1 mark each)*
2. Write short notes on the following:
- (i) Corporate Dividend Tax
 - (ii) Tax Evasion *(5 marks each)*
3. (a) Under what circumstances can an assessee appeal to the Appellate Tribunal. *(5 marks)*
- (b) What do you understand by "Book Profit" in the context of Minimum Alternate Tax. *(5 marks)*

PART B - INDIRECT TAXATION – LAW AND PRACTICE

4. (a) Choose the most appropriate answer from the given options in respect of the following:
- (i) For the purpose of central excise, the following is a 'Manufacture' -
 - (a) Cutting and polishing of diamonds
 - (b) Filtration/purification of commercial grade castor oil
 - (c) Testing and quality control
 - (d) Making coffee beans from raw coffee berries.
 - (ii) Interest under section 11BB for interest on delayed refunds will be payable for the period beyond _____ from the date of receipt of application upto date of refunds.
 - (a) 3 months
 - (b) 6 months
 - (c) 4 months
 - (d) 1 Year
 - (iii) In the case of cigarettes, the assessment will be done by:
 - (a) Assessee
 - (b) Assistant Commissioner
 - (c) Superintendent
 - (d) Any of the above

- (iv) The Daily Stock Account shall be preserved for a period of _____ immediately after the financial year to which such records pertain.
- (a) 8 years
 - (b) 3 years
 - (c) 5 years
 - (d) 4 years
- (v) For the contravention of the provisions for which no penalty has been provided in the Cenvat Credit Rules, 2004 then assessee shall be liable to a penalty which may extend to rupees:
- (a) 10,000
 - (b) 8,000
 - (c) 5,000
 - (d) 15,000
- (1 mark each)*
- (b) State with reasons in brief, whether the following statements are true or false:
- (i) In case of captive consumption of goods for production of other article by the assessee, the value will be 125% of cost of production.
 - (ii) Any article which is imported into India shall, in addition, be liable to a duty equal to the excise duty for the time being leviable on a like article, that duty is called Safeguard duty.
 - (iii) The goods may remain in warehouse till the expiry of 5 years in case of Capital goods for use by 100% EOU.
 - (iv) The Advance Ruling as provided under the Customs Act, 1962 should be given within a time limit of 60 days from the date of receipt of application:
 - (v) As per the Customs Act, 1962 condonation of delay by commissioner (Appeals) on sufficient cause being shown can be given for a further period of 45 days.
- (1 mark each)*
- (b) Write Short Notes on the following:
- (i) Trade Parlance theory
 - (ii) Harmonised System of Nomenclature
- (5 marks each)*
5. (a) What are the clearances whose values are excluded for the purpose of calculating the Small Scale Exemption Limit (SSI) while calculating the turnover of Rs.150/400 lakhs? *(5 marks)*
- (b) State the situation in which an order of an adjudicating authority becomes appealable in Customs Law. *(5 marks)*
- (c) Explain the provision for claiming drawback of duty paid on imported goods when they are re-exported. *(5 marks)*

6. (a) Having regard to the provisions of section 4 of the Central Excise Act, 1944, compute/derive the assessable value of excisable goods, for levy of duty of excise, given the following information:

- Cum-Duty wholesale price including sales tax of Rs.2500	15,000
Normal secondary packing cost	1,000
Cost of special secondary packing	1,500
Cost of durable and returnable packing	1,500
Freight	1,250
Insurance on freight	200
Trade discount (normal practice)	1,500
Rate of Central Excise duty as per Central Excise tariff	10% Adv.
	<i>(10 marks)</i>

- (b) What do you understand by "Doctrine of Unjust Enrichment".
(5 marks)

PART C – INTERNATIONAL TAXATION

7. (a) State with reasons in brief, whether the following statements are true or false:
- Uncontrolled transaction means a transaction between enterprises other than associated enterprises.
 - A tax heaven is a place where there is no tax on income or it is taxed at low rated of tax structure.
 - The application of Advance Ruling may be withdrawn within 45 days from the date of application.
 - The amount of income tax shall in case of foreign company be increased by a surcharge @ 5 per cent.
 - CFC stands for Controlled Fund Corporation. *(1 mark each)*
- (b) What is Transfer Pricing? Explain it with reference to relevant provisions of the Income Tax. *(5 marks)*
- (c) Explain the Authority for Advance Rulings under the Income Tax Act, 1961? Who can seek Advance Ruling? *(5 marks)*
- (d) What do you mean by foreign tax credit? *(3 marks)*
- (e) What do you mean by Double Taxation Avoidance Agreements (DTAAs). *(2 marks)*
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PROFESSIONAL PROGRAMME
ADVANCED TAX LAWS AND PRACTICE

QUESTION PAPERS OF PREVIOUS SESSIONS

Question papers of immediate past two examinations of Advanced Tax Laws and Practice paper are appended to this study material for reference of the students to familiarize with the pattern and its structure. Students may please note that answers to these questions should not be sent to the Institute for evaluation.

DECEMBER 2011

Time allowed : 3 hours

Maximum marks : 100

NOTE : *All references to sections mentioned in Part-A of the Question Paper relate to the Income-tax Act, 1961 and relevant Assessment Year 2011-12, unless stated otherwise.*

PART A

(Answer ANY TWO questions from this part)

1. (a) Sure Success Ltd. wants to acquire an asset costing ₹1,00,000. It has two options available, the first one is buying the asset by taking a loan repayable in five installments of ₹20,000 each with 14% interest per annum. The second is leasing the asset for which annual lease rental charge is ₹30,000 upto 5 years. The lessor charges 1% as processing fee in the first year. Assume the internal rate of return to be 10%. The present value factors are —

Year	1	2	3	4	5
P/V factor	.909	.826	.751	.683	.621

Assuming that the payments are made at the end of the year, suggest which alternative is better for the company. The rate of depreciation is 15% while tax rate is 33.22%. *(10 marks)*

- (b) What is the difference between 'demerger' and 'slump sale' ? *(5 marks)*
2. (a) Royal Ltd. commenced operations of the business of a new five star hotel in Mumbai on 1st April, 2010. The company incurred capital expenditure of ₹600 lakh on purchase of land and ₹95 lakh on construction of building during the period from January, 2010 to March, 2010 exclusively for the above business, and capitalised the same in its books of account as on

1st April, 2010. Further, during the previous year 2010-11, it incurred capital expenditure of ₹10 crore (out of which ₹60 lakh was for acquisition of land) exclusively for the above business.

Compute the deduction under section 35AD for the assessment year 2011-12, assuming that Royal Ltd. has fulfilled all the conditions specified in section 35AD and has not claimed any deduction under chapter VI-A under the heading 'C-Deductions in respect of certain incomes'.

(6 marks)

- (b) Conversion of small private companies and unlisted public companies into limited liability partnership is exempt from capital gains tax subject to fulfillment of certain conditions. State these conditions as specified in section 47(xiiib). (6 marks)
- (c) Discuss tax implications of dividend declaration and issue of bonus shares. (3 marks)
3. An employee is going to join your company on annual CTC of ₹18,00,000. Prepare a remuneration plan for him keeping in view the following :
- (i) He wants to minimise his tax liability within the legal framework but take home salary should not be less than ₹9 lakh.
- (ii) He does not own a house.
- (iii) He owns a car. But he can take another car from the company.
- (iv) He has two children and one of them is in a boarding school.
- (v) His wife is employed and she gets children education allowance.
- (vi) There is no uniform code in your company. (15 marks)

PART B

(Answer Question No.4 which is **COMPULSORY** and **ANY TWO** of the rest from this part.)

4. (a) Write the most appropriate answer from the given options in respect of the following :
- (i) Which of the following has not been expressly defined under the Central Excise Act, 1944 —
- (a) Broker
(b) Goods
(c) Curing
(d) Factory.
- (ii) Which of the following scheme is optional under central excise —
- (a) Duty based on tariff value
(b) Duty based on MRP
(c) Duty based on transaction value
(d) Duty based on compounded levy.
- (iii) Under section 23 of the Customs Act, 1962, duty payable is remitted

if imported goods are lost, destroyed or abandoned before —

- (a) Goods are examined
 - (b) Duty has been paid
 - (c) The proper officer has made an order for clearance
 - (d) Goods are cleared for home consumption.
- (iv) A proper tax planning exercise would have to take into consideration the following aspect(s) under the Customs Act, 1962 —
- (a) Classification of goods
 - (b) Valuation of goods
 - (c) Exemption notifications
 - (d) All of the above.
- (v) Effective rate of customs duty on baggage is —
- (a) 36.05%
 - (b) 41.2%
 - (c) 30.9%
 - (d) 51.5%. *(1 mark each)*

(b) Rewrite the following sentences after filling-in the blank spaces with appropriate word(s)/figure(s) :

- (i) The _____ is not eligible to take credit of special CVD paid on imported goods under section 3(5) of the Customs Tariff Act, 1975.
- (ii) Order of CESTAT relating _____ to can be appealed directly to the Supreme Court of India under section 35L of the Central Excise Act, 1944.
- (iii) If fuel or lubricating oil is supplied as stores to foreign going vessel, _____ customs duty paid on the fuel or lubricating oil is refunded as duty drawback.
- (iv) Assessee can apply for settlement _____ in lifetime of applicant except in respect of some specified cases.
- (v) The doctrine of promissory estoppel has its origin in principles of _____.
(1 mark each)

(c) Test the veracity or otherwise of the following assertions:

- (i) There can be 'manufacture' even if both inputs and final product fall under same tariff heading.
- (ii) Mere change in tariff does not mean there is 'manufacture'.

(3 marks each)

(d) Can a show-cause notice be issued within a period of five years from the relevant date if the internal audit party finds during the audit of central excise records of a manufacturer that central excise duty has been short paid? Explain.
(4 marks)

5. (a) Solid Shoes Co., a manufacturer of footwear, used to purchase various raw materials like fabrics, rubber, chemicals, solvent, etc., which were mixed together. The thin layer of such mixture was sandwiched between

two sheets of textile fabric through a calendaring machine. The resultant product 'Double Textured Rubberized Fabric' (DTRF) was cut and stitched as per requirement and was used as shoe-uppers. At times, DTRF was sent to job-workers for stitching purposes. After completing the entire process, the vulcanisation of footwear was done and then, it would be available for sale as footwear.

Some of the DTRF was used in the manufacture of canvas shoes, which were exempt from duty. The department contended that the intermediate product DTRF was a distinct product with specific properties and was used in considerable quantities for making rain-coats, holdalls, hand-bags, etc., in the outside market. Since the DTRF was excisable good and it was used in the manufacture of exempted final product being canvas shoes, therefore DTRF was liable to excise duty. However, the department didn't have sufficient evidence to prove its marketability.

Examine whether contention of the department is correct by referring to case law, if any, in the light of explanation added to section 2(d) of the Central Excise Act, 1944 w.e.f. 10th May, 2008. (5 marks)

- (b) Improper Ltd. made an unauthorised import of goods, which were later on confiscated. Goods were not redeemed by paying fine under section 125 of the Customs Act, 1962. The assessee contended that once the imported goods were confiscated and the option to release them was not exercised, no duty was payable. It placed reliance on section 23 of the said Act which provides that if the owner of imported goods relinquishes his title to the goods, he shall not be liable to pay the duty thereon.

Discuss briefly whether the assessee is bound to pay customs duty with reference to decided case law, if any. (5 marks)

- (c) Explain the interpretation of phrase 'a mistake apparent from record' as mentioned in section 35C(2) of the Central Excise Act, 1944. (5 marks)

6. (a) Unfair Ltd. sold 100 units manufactured by it for ₹12,000 per unit. It had received interest-free advance of ₹6,00,000 from the buyer for the whole of the year. Compute the assessable value of 100 units sold in following independent cases :

- (i) The price charged from other buyers is ₹11,600 per unit.
- (ii) The price charged from other buyers is ₹12,800 per unit.
- (iii) The normal rate of interest is 12% per annum and the price charged from other buyers is ₹12,800 per unit. (6 marks)

- (b) From the following information, compute the total amount of customs duty payable by the importer :

- (i) Assessable value under customs : ₹6,00,000.
- (ii) Tariff value notified under section 3(2) of the Central Excise Act, 1944 for payment of excise duty on like article manufactured in India: ₹5,00,000.
- (iii) Basic customs duty= 10%
Central excise duty = 10%

Special CVD = Nil
 Education cess = as applicable. (6 marks)

- (c) Mayank manufactured and exported goods worth ₹10,00,000 to Uday of UK on 1st January, 2011 and availed duty drawback of ₹15,000. Mayank imported the same goods on 8th February, 2011. What will be the customs duty payable by Mayank, if rate of basic customs duty is 10% and goods are exempt from CVD and special CVD ? (3 marks)
7. (a) Besides excise duty concessions, what are the other procedural concessions enjoyed by small scale industries ? Explain briefly. (7 marks)
- (b) Discuss briefly the provisions of section 28(5) of the Customs Act, 1962 regarding conclusion of proceedings at show-cause notice stage itself, when extended period of limitation has been invoked. (5 marks)
- (c) Write a note on 'refund of export duty'. Is doctrine of unjust enrichment applicable to it? (3 marks)

PART C

8. Attempt *any five* of the following:

- (i) What are the factors to be considered in taking decision whether a country is tax haven or not? (4 marks)
- (ii) Ajit has an undertaking (Unit-A) in free trade zone (FTZ) and another undertaking (Unit-B) in domestic tariff area (DTA). From the following particulars, compute the deduction under section 10A for the assessment year 2011-12 :

	<i>Unit-A</i> (₹)	<i>Unit-B</i> (₹)
Total turnover	60 lakh	40 lakh
Export turnover (included in above)	40 lakh	—
Profit earned	21 lakh	12 lakh

(4 marks)

- (iii) Explain in brief the circumstances under section 9(1)(v), (vi) and (vii) when interest, royalty and fees for technical services (FTS) shall be deemed to accrue or arise in India. (4 marks)
- (iv) Who can seek 'advance rulings'? (4 marks)
- (v) Discuss when an enterprise is taken as 'associated enterprise' under section 92A. (4 marks)
- (vi) Discuss the salient aspects concerning permanent establishment. (4 marks)



JUNE 2012*Time allowed : 3 hours**Maximum marks : 100*

NOTE : All the references to sections mentioned in Part-A of the Question Paper relate to the Income-tax Act, 1961 and relevant Assessment Year 2012-13, unless stated otherwise.

PART A*(Answer ANY TWO questions from this part.)*

1. (a) State, with reasons in brief, whether the following statements are true or false :
- (i) The minimum penalty for failure to get accounts audited under section 44AB or furnish audit reports along with return of income is ₹1 lakh and is imposed by the assessing officer.
 - (ii) The minimum penalty for failure to deduct tax at source or failure to pay wholly or partly the tax under section 115-O(2) or second proviso to section 194-B is a sum equal to the amount of tax failed to be deducted or paid.
 - (iii) A non-resident company's tax liability arises in India when the resident company credit the royalty payable for the amount due before making payments to it outside India based on the contract which was signed and executed outside India.
 - (iv) It is mandatory for a corporate assessee to file a return in electronic form even if there is a loss or nil income as per section 139(1) read with section 139D.
 - (v) The law declared by the Supreme Court upon a judgment of a High Court is binding on that High Court only. *(2 marks each)*
- (b) "Assets which are included in the definition of 'intangible assets' under section 32(1)(ii) include, along with other things, any other business or commercial rights of similar nature; goodwill, when appositely understood, does convey a positive reputation built by a person/company/business concern over a period of time and hence, it is an asset, eligible to depreciation."
- Critically examine the proposition stated in the above para. Support your answer with relevant case law. *(5 marks)*
2. (a) Lucent Ltd. purchased a machinery on 1st April, 2011 for ₹10 crore by availing 70% loan facility from bank. The machine was put to use into effective production on 1st February, 2012. The interest on loan works out to 12% per annum. Advise Lucent Ltd. on the treatment of interest payment made on this loan and depreciation allowable for the previous year 2011-12. You may assume that this is the only machine in its block. *(5 marks)*
- (b) Various houses owned by the assessee-company were allotted for the

residential purposes to its employees having salaries less than ₹5 lakh per annum. The company claimed wealth-tax exemption in respect of the said houses (including the land appurtenant comprising of garden, pathway, tennis court, etc.). The department has denied such exemption. Examine whether the action of the department is tenable in law ? Cite relevant case law. (5 marks)

- (c) Can the Appellate Tribunal rectify the mistake in the following separate cases —
- (i) if a different interpretation of law is available.
 - (ii) if a retrospective amendment is made to the provision.
 - (iii) if a subsequent decision of the Supreme Court is available on the subject after the Appellate Tribunal's order.
 - (iv) if a ruling cited before the Appellate Tribunal is not considered.
 - (v) if fresh grounds are raised before the Appellate Tribunal.

(1 mark each)

3. What is the difference between 'minimum alternate tax' under section 115JAA and 'alternate minimum tax' under section 115JC ? Who is subject to these taxes ? Also discuss the implication of these taxes in the case of an overseas entity having a permanent establishment (PE) in India. (15 marks)

PART B

(Answer Question No.4 which is **COMPULSORY** and **ANY TWO** of the rest from this part.)

4. (a) Write the most appropriate answer from the given options in respect of the following :
- (i) What is the source of power of levying VAT under the Constitution of India —
 - (a) Entry 84 of List I
 - (b) Entry 97 of List I
 - (c) Entry 52 of List II
 - (d) Entry 54 of List II.
 - (ii) National Calamity Contingent Duty of customs is not imposed on —
 - (a) Mobile phones
 - (b) Pan masala
 - (c) Chewing tobacco
 - (d) Cigarettes.
 - (iii) What is the amount of prescribed fees which should be accompanied with an application to settlement commission —
 - (a) ₹500
 - (b) ₹1,000
 - (c) ₹2,500
 - (d) ₹5,000.

- (iv) Section 114 of the Customs Act, 1962 provides for levy of penalty in case of goods in respect of which any prohibition is in force not exceeding —
- One time of the value of the goods
 - Three times of the value of the goods
 - Two times of the value of the goods
 - Four times of the value of the goods.
- (v) Credit balance as on 31st January, 2012 is ₹75,000 and on 5th February, 2012 it is ₹87,000. Duty payable for January, 2012 is ₹90,000. How much credit can the assessee utilise from the CENVAT credit account —
- ₹87,000
 - ₹75,000
 - ₹37,500
 - ₹43,500. (1 mark each)
- (b) Re-write the following sentences after filling-in the blank spaces with appropriate word(s)/figure(s) :
- Service tax is a _____ based consumption tax on commercial activities.
 - Residual penalty for violation of CENVAT Credit Rules can be imposed _____ under Rule 15A of CENVAT Credit Rules, 2004.
 - Refund of export duty under section 26 of the Customs Act, 1962 is _____ provisions of unjust enrichment.
 - Promissory estoppel plea fails where _____ intervenes.
 - _____ means the value of imported goods determined in accordance with Rule 8 of Customs Valuation (Determination of Price of Imported Goods) Rules, 2007. (1 mark each)
- (c) State whether the following goods are 'input' as per Rule 2(k) of the CENVAT Credit Rules, 2004 :
- All goods used for generation of electricity for captive use
 - Light diesel oil
 - Motor vehicles
 - Goods used for making of structures for support of capital goods
 - Goods used for providing free warranty for final products. (1 mark each)
- (d) Pradhan imported a consignment valuing ₹8 lakh vide a bill of entry presented before the proper officer on 25th April, 2011 on which date the rate of customs duty was 10%. On Pradhan's failing to produce requisite documents for the purpose of assessment, the goods were provisionally assessed at a value of ₹8 lakh and the duty was paid accordingly on the

same date. The goods were finally assessed at ₹12 lakh on 9th June, 2011 and the differential duty was paid on 12th June, 2011.

Compute the amount of interest, if any, under section 18 of the Customs Act, 1962. (5 marks)

5. (a) Avon Plastic Ltd. is a company manufacturing plastic goods. It has two factories — one at Jaipur and another at Noida. Following information in respect of the two factories is available for the financial year 2011-12:

(₹ in lakhs)

Particulars	Jaipur Factory	Noida Factory
(i) Goods cleared with own brand name	75	100
(ii) Clearances of plastic containers bearing brand name of Jolly Jams (to pack jam by them)	45	70
(iii) Goods cleared to 100% EOU against Form CT-3	90	80
(iv) Export to Bhutan	50	60
(v) Job work under Notification No.214/86-CE dated 25.03.1986	65	55
(vi) Job work under Notification No.84/94-CE dated 11.04.1994	85	95

On the basis of above information, you are required to ascertain whether Avon Plastic Ltd. is eligible for the benefit of small scale exemption under Notification No.8/2003-CE dated 1st March, 2003 during the financial year 2011-12. (6 marks)

- (b) From the following information, compute the amount of basic customs duty and additional duty of customs payable under section 3(1) of the Customs Tariff Act, 1975 in respect of import of readymade garments:

- Assessable value under customs : ₹1,50,000;
- Tariff value notified under central excise for levy of excise duty: 45% of the retail sale price;
- Retail sale price : ₹4,00,000 (readymade garments are not notified under section 4A of the Central Excise Act, 1944);
- Basic customs duty : 10%;
- Central excise duty : 10%; and
- Education cess : as applicable. (5 marks)

- (c) Vishal has made an unauthorised import of 1,000 pieces of a product. Other particulars are as under :

Total assessable value	:	₹ 5,00,000
Total customs duty payable	:	₹ 1,20,000
Market price in India	:	₹ 1,000 per piece

Customs authorities have confiscated the said goods and importer has been given an option to get the said goods released on payment of a fine equal to margin of profit.

Compute — (i) amount of fine payable; and (ii) maximum amount of fine under section 125 of the Customs Act, 1962. *(4 marks)*

6. (a) Menz Car Co. is manufacturing cars and discharging duty liability thereon by including cost of mandatory one year warranty in the transaction value of cars. An option was given to customers to obtain extended warranty for a further period of two years against payment of separate charges. This extended warranty was introduced by assessee and administered through dealers for which dealers were allowed commission. Such extended warranty charges were not included in assessable value.

The department contended that the same were includible in assessable value of manufactured cars. Discuss, in the light of decided case law, if any, whether contention of the department is tenable in law. *(5 marks)*

- (b) Explain the validity of the following statements with reference to Chapter IX of the Customs Act, 1962 containing the provisions relating to warehousing :

(i) Owner of any warehoused goods cannot carry on any manufacturing process or other operations in relation to warehoused goods.

(ii) Warehoused goods may be transferred from one warehouse to another warehouse.

(iii) The importer must execute a bond equal to the amount of duty assessed with necessary surety or security. *(2 marks each)*

- (c) Briefly discuss whether the following powers vest with the Commissioner (Appeals) under the Central Excise Act, 1944/Customs Act, 1962 :

(i) Remanding the case back to the adjudicating authority; and

(ii) Condoning the delay in filing appeal before him. *(2 marks each)*

7. (a) What are the goods notified under section 3A of the Central Excise Act, 1944 liable to duty based on annual capacity of production ? Whether declaration of retail sale price is mandatory in case of such notified goods? *(5 marks)*

- (b) Briefly explain with reference to section 11AC of the Central Excise Act, 1944 the circumstances under which penalty has to be imposed mandatorily. State whether it can be reduced statutorily. *(5 marks)*

- (c) Discuss the provisions of the Customs Act, 1962 relating to the determination of duty where imported goods consist of articles liable to different rates of duty. *(5 marks)*

PART C

8. Attempt **any two** of the following:

(i) You are a tax consultant to an overseas manufacturing company which is

going to start a permanent establishment in India with manufacturing facility in Madurai District of Tamilnadu. Prepare a report for the Chairman of the company highlighting latest transfer pricing provisions applicable in India. *(10 marks)*

- (ii) Explain the provisions relating to 'advance ruling' in the Income-tax Act, 1961. *(10 marks)*
 - (iii) How foreign institutional investors are taxed on the income and capital gains arising from the transfer of securities ? *(10 marks)*
-